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ABSTRACT

Forty-six working papers for presentation at a research forum on public policy and philanthropy are presented. Thirteen sections include the following topics: (1) looking forward to the year 2000: public policy and philanthropy (e.g. "Rationales for Tax Exemption," by Harvey P. Dale); (2) shifting boundaries among the sectors (e.g. "The Shifting Boundaries of the Independent Sector," by Jon Van Til); (3) accountability issues (e.g. "Accountability of the Independent Sector," by Marion R. Fremont-Smith); (4) public policy and nonprofit organizations (e.g. "Advocacy Movements for Children Since 1960," by Robert H. Bremner); (5) values and ethics (e.g. "Motivations for Giving and Voluntary Service," by Eugene J. Webb and Morris E. Eson); (6) demographic trends and new information about the sector (e.g. "The Future World of Work: Impact on the Independent Sector," by Linda J. Forbes); (7) philanthropy, public policy and the poor (e.g. "Public Needs, Private Response: Patterns in the Eighties," by Donna L. Chmielewski); (8) financing nonprofit organizations (e.g. "The Prospects for Volunteering Over the Next Five Years," by Robert J. O'Connor and Rebecca S. Johnson); (9) regional and community issues (e.g. "Regional Generosity and Civic Commitment," by Julian Wolpert); (10) public policy among major subsectors (e.g. "Private Higher Education: Public Policy and the Competition Issue," by Margot Stern Strom and Alan L. Stoskopf); (11) the nonprofit sector abroad (e.g. "The Public Sector and the Private: Organizational Choice and the Third Sector in Europe," by Helmut K. Anheir); (12) issues in corporate giving (e.g. "Cause-Related Marketing: Here to Stay or a Passing Fad?" by Kathleen A. Krentler); and (13) foundation issues and public policy (e.g. "Foundations and the Shaping of Public Policy," by James A. Smith). (SM)

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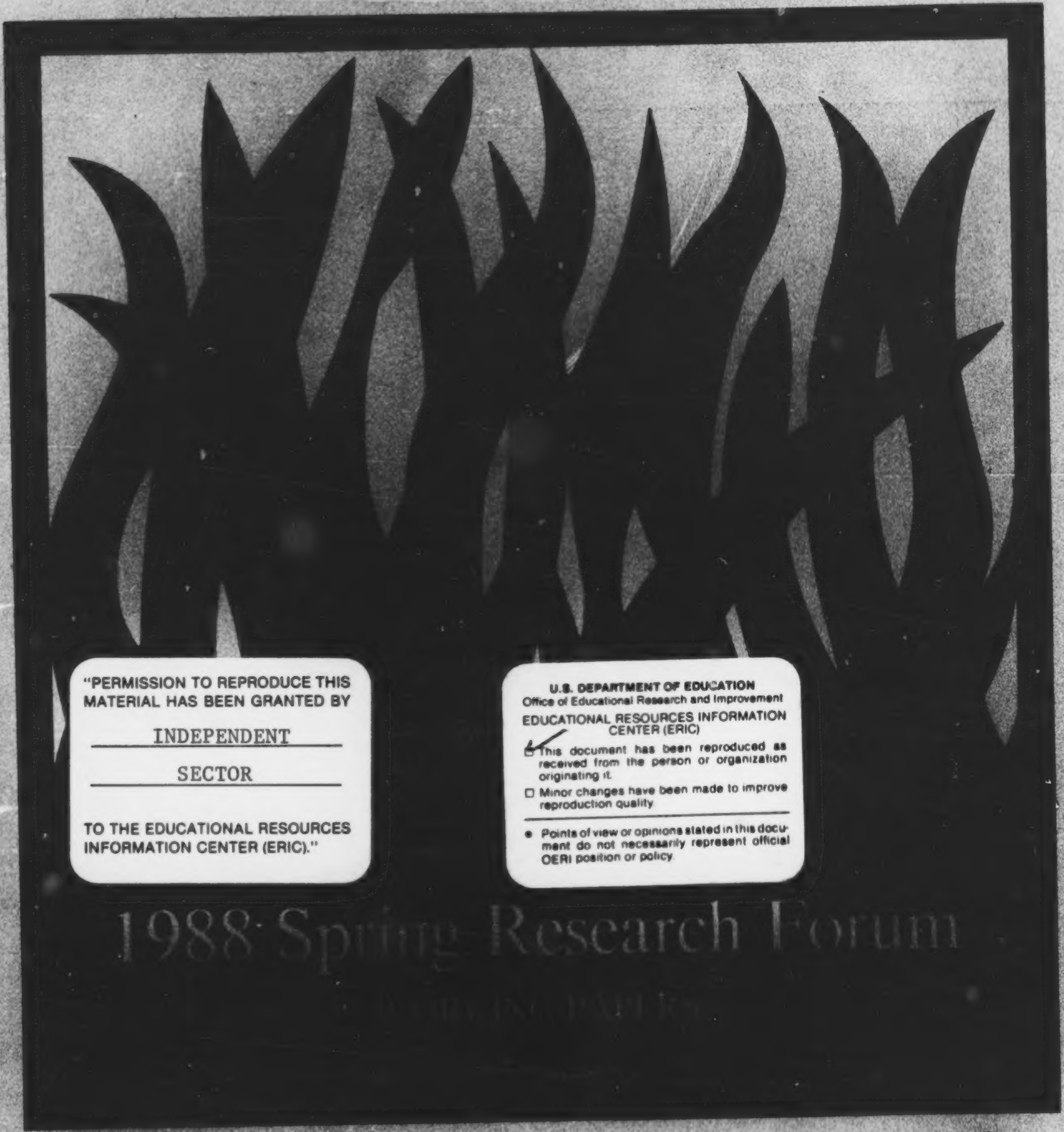
Looking Forward to the Year 2000: Public Policy and Philanthropy



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1988 Spring Research Forum

WORKING PAPERS

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INDEPENDENT SECTOR

UNITED WAY INSTITUTE

*Looking Forward to the Year 2000:
Public Policy and Philanthropy*

Spring Research Forum
WORKING PAPERS

March 17-18, 1988

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FOREWORD

These Working Papers have been prepared for the 1988 Spring Research Forum, entitled "Looking Forward to the Year 2000: Public Policy and Philanthropy." The Forum, co-sponsored by INDEPENDENT SECTOR and the United Way Institute, will be held on March 17-18, 1988 at the Meridien Hotel in San Francisco.

Over the past three decades, the public perceptions of the independent sector have been changing. By independent sector, we mean all voluntary organizations, including advocacy organizations, private non-profit institutions (hospitals and health organizations, schools, research organizations, museums, and religious institutions), and human (social) services organizations. Also included are the whole range of institutions serving the environment, international aid and development, community development, public education, and foundation and corporate development, public education, and foundation and corporate social responsibility programs.

Both the nonprofit, charitable sector and for-profit service industries have grown enormously. Part of this year's Spring Research Forum will address the changes reflected in a variety of public policy issues and challenges ranging from the definition of tax exempt status, the rights of organizations receiving government funds to advocate certain policies, the definition of certain nonprofits, the competition between nonprofits and small business, and varying analyses relating to the "blurring" of distinctions among nonprofits, government, and business.

Richard W. Lyman, President of the Rockefeller Foundation, and former President of Stanford University, will deliver the keynote address on March 17th.

The diversity and breadth of this year's Working Papers reflect the growing scholarly interest in the independent sector. It is with particular pleasure that we can provide in these papers the first results of research projects currently underway or just completed. Much of the information included here has not been published elsewhere.

The first section includes papers for the General Session on March 18, "Looking Forward to the Year 2000: Public Policy and Philanthropy." Panel discussions will cover twelve topical areas, including: 1) Shifting Boundaries Among the Sectors; 2) Accountability Issues; 3) Public Policy and Nonprofit Organizations; 4) Values and Ethics; 5) Demographic Trends and New Information About the Sector; 6) Philanthropy, Public Policy, and the Poor; 7) Financing Nonprofit Organizations; 8) Regional and Community Issues; 9) Public Policy Among the Major Subsectors; 10) The Nonprofit Sector Abroad; 11) Issues in Corporate Giving; and 12) Foundation Issues and Public Policy.

Authors were all asked to consider three questions on their topics: 1) What are the current trends in each of the specific theme areas?; 2) What will result if current policies and/or practices are maintained?; and 3) What other policies or practices should be considered? Through these papers and the Forum sessions, we hope to expand and extend the development of a basic body of knowledge on the nonprofit sector and its role and functions in American society.

The panel sessions are intended to provide an opportunity for authors and attendees to discuss research in detail. We urge you to review papers on topics of special interest to you and to prepare questions for the discussion sessions. The authors will not present their papers at the panel sessions, but will be prepared to discuss the issues raised in their papers.

After reviewing the Working Papers, registrants are asked to select three to six areas of particular interest in order to plan their panel attendance.

Finally, we would like to thank the authors who agreed to make contributions and observed stringent deadlines. The opinions expressed are those of the authors and not necessarily those of INDEPENDENT SECTOR or of the United Way Institute. The contributions of these authors provide us with an important framework for charting the research map on the role and functions of the independent sector and its societal impact both in the United States and abroad. Their work also will provide direction for future researchers in the years ahead.

We look forward to meeting you in March.

Virginia A. Hodgkinson
Vice President, research
INDEPENDENT SECTOR

Russy D. Sumariwalla
Vice President
United Way of America

SECTION ONE:

LOOKING FORWARD TO THE YEAR 2000: PUBLIC POLICY AND PHILANTHROPY

Rationales for Tax Exemption

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The Two Independent Sectors

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Budget Neutral Options to Encourage Charitable Giving

by Lawrence B. Lindsey 25

WORKING DRAFT

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RATIONALES FOR TAX EXEMPTION

by

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Prepared for the 1988 Spring Research Forum
"Looking Forward to the Year 2000:
Public Policy and Philanthropy"

San Francisco, California
March 17-18, 1988

Introduction

This paper has three aims. First, it contains a brief description of various rationales which purport to justify or explain the granting of tax exempt status to certain organizations.[1] The aim is *not* to set forth a thorough exegesis, but rather merely a precis, of these rationales. The risk of distortion through oversimplification is real.

Second, it will venture a few select observations or criticisms of some of the theories. Here, again, the goal is to be brief rather than comprehensive. For the sake of clarity, any observations or criticisms follow directly after the description of each particular rationale.

Third, it suggests that no single rationale can or should be expected to explain or justify tax-exempt status. The not-for-profit sector of our society is complex and varied; its lineage is ancient. It would be unreasonably simplistic to expect to capture its essence or justification within the compass of any theory.

It does not follow that exploring such rationales is a waste of time. The exploration may help prevent uncritical acceptance of any particular theory. By pondering the limits of these justifications, by seeking out their weaknesses, we may better understand their proper force; we may become better-balanced advocates of our positions; we may better perceive the strengths of the positions of our opponents.

Rationales for Tax Exemption

The legal literature discussing tax-exemption rationales is not voluminous.[2] A number of different justifications for exempting nonprofit organizations from the income tax may be gleaned from a perusal of the principal writings. Five such theories are discussed briefly, in no particular order, below.[3]

First, tax-exempt status may be justified because the activities of the nonprofit sector are direct replacements for governmental obligations. The notion is that government should not tax organizations, thus reducing their ability to deliver goods and services by the amount of the tax, when that reduction merely creates a vacuum which must be filled by the government itself.[4] Stated another way, a deal has been struck: tax exemption in exchange for the private fulfillment of governmental duties.

This theory may be criticized on several grounds: (1) it fails to explain why tax exemption is not granted to *for*-profit providers of the same goods and services;[5] (2) it cannot explain the tax exemption of churches and religious organizations, since the First Amendment forbids government from intruding into those areas;[6] and (3) the amount of the tax-exemption benefit is not related to the value of goods or services provided, but rather to the amount of capital or retained earnings of the organization;[7] (4) the theory does not support tax exemption, but merely argues that tax exemption is one of tow routes for the provision of the desired goods and services.[8] Despite these criticisms, this first rationale remains the most "popular" and oft-repeated justification for tax exemption.

Second, tax-exemption may be justified because of the way nonprofit organizations contribute to pluralism. The notion is that such organizations provide goods and services for the public, but perhaps more efficiently and in any event with more diversity than the government.[9]

Possible criticisms include: (1) it is not clear how to measure efficiency; some would dispute the claim that not-for-profit entities are more efficient than government, at least in all instances; lacking an agreed gauge, it is impossible to rely on that criterion;[10] (2) the argument from pluralism proves too much, because for-profit firms could also claim it;[11] (3) the justification does not provide useful guidelines for decision-makers trying to draw lines between various forms of and limits on tax exemption.[12]

Third, tax exemption may be explained by the inappropriateness of applying customary measures of "income" to not-for-profit entities.[13] Critics could counter: (1) the difficulty of defining an appropriate tax base argues for better or specially-crafted definitions, not exemption; (2) the problems may be overstated; at least a good portion of the receipts of non-profits respond fairly well to ordinary notions of "income."[14]

Fourth, the exemption may be justified on the grounds that taxing the not-for-profit indirectly would impose the tax burden on its customers and beneficiaries, but without taking into account their ability to pay.[15] Critics could respond: (1) tax rates imposed on entities, even in the business world, are not selected on the basis of the ability of the entities' customers to pay;[16] (2) in many cases, the ability-to-pay criterion would be met: in the case of "donative" nonprofits by the joint "contributions" of donors and customers, and in the case of "commercial" nonprofits by their typically-affluent customers;[17] (3) in any case, the true incidence of an entity-level income tax is a much-debated and uncertain question;[18] (4) the tax-exemption benefit itself fails to take into account the ability to pay of the entity's customers; the benefit is closely related to the retained "capital" of the entity rather than the nature of its clientele.[19]

Fifth, the exemption may be based on the joint presence of "contract failure" and insufficiency of capital. This rationale,

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espoused somewhat gingerly by Prof. Hansmann,[20] is by far the most difficult to encapsulate; it is also perhaps the most satisfactory current contender among these theories. It deserves a slightly enlarged description. It proceeds from two notions. First, Prof. Hansmann postulates that many "commercial" nonprofits operate in industries characterized by "contract failure," i.e., in which customers are unable to "make accurate judgments about the quality, quantity, or price of services provided by alternative producers."[21] Second, Prof. Hansmann argues that certain nonprofit organizations have severe restraints on their ability to raise capital, unlike for-profit organizations which can readily borrow or issue stock.[22] When both criteria are met, i.e., when an industry is characterized by contract failure and nonprofits in that industry have substantial needs for capital, tax exemption may be justified as "a crude mechanism for subsidizing capital formation . . . ."[23]

Several criticisms may be made: (1) the rationale is, admittedly, "crude," since the value of the tax exemption is not well related to the goals sought; (2) it is not clear that it is wise to facilitate the aggregation of capital in the nonprofit sector, where it may be retained, free from tax and other means of diffusion;[24] (3) if the rationale were accepted, implementing legislation would almost certainly involve quite considerable complexity;[25] (4) granting tax exemption to a industry because it has trouble raising capital seems likely to promote economic inefficiency; (5) Prof. Hansmann's argument accepts as a given that an entity-level tax on income is appropriate (or at least inevitable) for business corporations; that premise gives away so much theoretical ground that there is not enough footing left to provide adequate support for a justification for sector-specific entity-level tax exemption.

Conclusion

At the outset, I promised a brief description and criticism of various rationales for tax exemption. I further proposed a thesis: that none of them is adequate to explain the rich variety of the not-for-profit sector. Instead, we must acknowledge that we are where we are not because of any prior rationale, but simply because that is the way we grew. Nor will any rationale adequately explain the growth pattern, since the tree has responded over time to all of the vagaries of human passions and conflicts.

In fairness, proponents of these rationales might agree that none is completely satisfactory. They might say that theories for tax exemption do not have as their primary goal an accurate description of the way things are. Rather, such theories are more helpful in providing guidelines for decisions about how things should be in the future. The various rationales can help legislators, regulators, and others to weigh alternatives for and evaluate possible changes in the tax treatment of not-for-profit entities. The failure of a theory to answer all questions does not prevent it from being useful in answering some questions.

These points have some force; various rationales have been, will be, and should be invoked as aids to reasoning, even if they do not resolve all conundrums. The logical gap is this -- if we concede that a given rationale is helpful in some, but not all, cases, how do we decide which cases fall in the former and which in the latter category? Either we need a still further theory to apply for that purpose, or we must resort to an appeal to "common sense" or "good judgment." I believe that no theory, and no theory of theories, will ever suffice to answer all of our current questions, much less future questions still unknown. We will always, finally, need to decide them without having any clearly-controlling formula to determine our course.

Oliver Wendell Holmes once said, "a page of history is worth a volume of logic."[26] Clearly we cannot understand or explain the scope of the tax-exemption privilege without studying history. History, however, is no more sufficient a guide than rationales; the future is not fully foretold by the past. It may be true, as Santayana said, that "[t]hose who cannot remember the past are condemned to repeat it."[27] But it is also true that, as Heraclitus is reputed to have opined nearly 500 years before the birth of Christ, "One cannot step twice into the same river."[28] And thus, again, looms the abyss -- although we may not rely on history alone as a guide, we lack comprehensive rules to instruct us when to deviate from prior experience in light of new conditions.

There is no solution to this inevitable dilemma. Indeed, in some sense we ought to embrace the uncertainty. If we are careful and thoughtful, our judgments will be both informed by history and influenced by at least some of the imperfect rationales scholars have advanced. Nevertheless, at the end of the day, our own minds and hearts will have to choose, and the choices will not always be clear. There will be room for vigorous disagreements. That too may be cause for celebration rather than consternation. If we truly believe in pluralism, we should embrace these opportunities with open minds and with intellectual honesty and rigor.

Thus, we must continue to study history. We must seek better rationales for our privileged status. We should not expect to find the Holy Grail; we should, rather, expect a quest without end. We cannot wait for final enlightenment, but must continue to make decisions as we go. As Learned Hand has told us, "life is made up of a series of judgments on insufficient data, and if we waited to run down all our doubts, it would flow past us."[29]

The ultimate goal is the exercise of thoughtful and informed judgments, rather than the elaboration of a comprehensive rationale. Theories are valuable not because they offer any realistic hope of all-inclusive solutions but because they provide grist for the mill of judgment. We should not expect total solutions; unrealistic expectations, unsatisfied, might be disheartening. We should instead stand fast on the uncertain ground of human judgment, informed by, but never totally constrained or determined by, even our best rationales and our most trenchant histories.

FOOTNOTES

1. An organization may be wholly or partially exempt from a wide variety of taxes, e.g., federal income or excise taxes, state or local income or property taxes. This paper addresses only exemption from federal income taxes, although qualification for such exemption often also results in exemption from other taxes.

The principal focus here is on entities described in Section 501(c)(3) of the Internal Revenue Code of 1986 [hereinafter I.R.C.], i.e., "main stream" charities. Many other sorts of organizations are wholly or partially exempt from federal income taxation, either by virtue of being described in other paragraphs of I.R.C. Section 501(c) or under a myriad of other provisions. For example, tax-exempt status is afforded to certain pension and profit-sharing trusts, farmers' and some other cooperative organizations, and foreign governments and their instrumentalities. Still other entities are generally free from income tax liability because their shareholders, beneficiaries, or partners are instead directly taxable on the entities' income, e.g., so-called S corporations, most partnerships, simple trusts, real estate investment trusts, and registered investment companies. The examples, in all cases above, are illustrative, not exhaustive. See B. HOPKINS, THE LAW OF TAX-EXEMPT ORGANIZATIONS 28-29 (5th ed. 1987), for others.

Because this paper generally does not discuss membership and mutual-benefit organizations, it also does not set out the quite-separate rationale for exempting their receipts from income taxation. That rationale is: the income tax should not be asserted against the entity, since the entity is merely a combination, pooling, or conduit for the activities of the various members. Payments by a group of neighbors to build and maintain a swimming pool for their common use would not have been taxed (nor would they have been deductible to those making the payments). Thus, their payments to a pool association should not attract an income tax. One court put it this way:

> "[W]here individuals have banded together to provide recreational facilities on a mutual basis, it would be conceptually erroneous to impose a tax on the organization as a separate entity. . . . No income of the sort usually taxed has been generated; the money has simply been shifted from one pocket to another, both within the same pair of pants. . . . [A]s to these funds the organization does not operate as a separate entity." McGlotten v. Connally, 338 F. Supp. 448, 458 (D.D.C. 1972).

Rationale

See Bittker & Rahdert, *infra* note 2, at 348-58; R. DESIDERIO & S. TAYLOR, *infra* note 2, at 4-16 - 4-18. This rationale is not free from problems. Indeed, it raises deep issues of why *any* entity which has members (i.e., shareholders, partners, beneficiaries) is subject to income tax. That line of inquiry would entail a discussion of so-called integration or imputation issues, and tax-incidence questions, which have been long debated with respect to the corporate income tax generally. Fortunately, it is outside the scope of this paper.

2. Among various sources consulted, the following seem particularly useful: Belknap, *The Federal Income Tax Exemption of Charitable Organizations: Its History and Underlying Policy* (1954), reprinted in IV RESEARCH PAPERS SPONSORED BY THE COMMISSION ON PRIVATE PHILANTHROPY AND PUBLIC NEEDS: TAXES 2025 (1977); Bittker & Rahdert, *The Exemption of Nonprofit Organizations from Federal Income Taxation*, 85 YALE L.J. 299 (1976); 1 R. DESIDERIO & S. TAYLOR, PLANNING TAX-EXEMPT ORGANIZATIONS section 4.03 (1987); Ellman, *Another Theory of Nonprofit Corporations*, 80 MICH. L. REV. 999 (1982); Hansmann, *The Rationale for Exempting Nonprofit Organizations from Corporate Income Taxation*, 91 YALE L.J. 54 (1981); B. HOPKINS, THE LAW OF TAX-EXEMPT ORGANIZATIONS ch. 1 (5th ed. 1987); McDaniel, *Federal Matching Grants for Charitable Contributions: A Substitute for the Income Tax Deduction*, 27 TAX L. REV. 377 (1972); McNulty, *Public Policy and Private Charity: A Tax Policy Perspective*, 3 VA. TAX REV. 229 (1984); Stone, *Federal Tax Support of Charities and Other Exempt Organizations: The Need for a National Policy*, 1968 U. SO. CAL. TAX INST. 27.

Several of the above articles are more centrally concerned with the policies affecting the deductibility of gifts to charities than with tax exemption of the charities themselves. The two questions are deeply intertwined. For example: "[T]he deduction allowed the donor is the counterpart of the exemption from income tax enjoyed by the charity itself [so that] the same policy decisions that justify the exemption for the charitable organization support the charitable contribution deduction." McNulty, *supra*, 3 VA. TAX REV. at 233; but see Hansmann, *supra*, at 72. Nevertheless, little effort has been made to plumb the depths of the relatively voluminous literature on the deduction. Furthermore, the scope of tax-exemption is not coterminous with the scope of the charitable deduction: many tax-exempt organizations are not eligible for tax-deductible gifts. The focus on legal literature reflects the background and training of the author, and should not be taken to suggest that other disciplines should be ignored; indeed, one of the main themes of this paper is that historical, economic, and other literature are often quite important.

Rationale

3. The author's enumeration is not free from question: not only might the various theories mentioned be organized or subdivided differently, but other possible justifications could be added to the list.

4. This is the rationale mentioned in the final report of the prestigious Filer Commission:

> "A frequently cited justification for tax immunities that affect nonprofit organizations is that government, in fact, would itself have to supply many of the services, fill many of the functions, of such organizations if they did not exist." REPORT OF THE COMMISSION ON PRIVATE PHILANTHROPY AND PUBLIC NEEDS, GIVING IN AMERICA: TOWARD A STRONGER VOLUNTARY SECTION 103 (1975).

Compare the following formulation:

> "Clearly then, the exemption for charitable organizations is a derivative of the concept that they perform functions which, in the organizations' absence, government would have to perform; therefore, government is willing to forego the otherwise tax revenues in return for the public services rendered." B. HOPKINS, *supra* note 2, at 5.

The same notion finds voice in Congressional reports, e.g., H. Rep. No. 1860, 75th Cong., 3d Sess. 19 (1939), and in court decisions, e.g., *McGlotten v. Connally*, 338 F.2d 448, 456 (D.D.C. 1972).

5. See, e.g., Hansmann, *supra* note 2, at 67-71.

6. The size of the church/religious sector is considerable. It accounts for almost half of the entire nonprofit universe, measured by amounts donated annually. See, e.g., AAFRC TRUST FOR PHILANTHROPY, GIVING USA: ESTIMATES OF PHILANTHROPIC GIVING IN 1986 AND THE TRENDS THEY SHOW 61-62 (1987) (over $40 billion donated to religious organizations and agencies in 1986). Other possible measures of its size are problematical due to the inaccuracy of available statistics and the difficulty of obtaining data from many of the organizations in question. See, e.g., V. HODGKINSON & M. WEITZMAN, DIMENSIONS OF THE INDEPENDENT SECTOR: A STATISTICAL PROFILE 106 (Independent Sector, 2d ed. 1986) ("The religion subsector presents a major problem for our estimates.") The zone proscribed by the First Amendment does not exhaust the areas in which the state would not act; there are many other sorts of entities whose functions would *not* be taken over by government should they cease to exist, yet to which tax exemption has always been afforded. See Belknap, *supra* note 2, at 2032-33:

> "[T]he quid pro quo explanation of tax exemptions . . . is not adequate as a justification of the privilege in some of the most important segments of the general area under discussion. . . . [T]he tax exemption privilege has much deeper roots than the quid pro quo theory would admit."

7. See, e.g., Hansmann, _supra_ note 2, at 71. A quite similar criticism, directed at the mismatch resulting from the use of _property_ tax exemption as a means of encouraging educational activities, is put forth in Note, _Alternatives to the University Property Tax Exemption_, 83 YALE L.J. 181, 183 (1973).

8. See Bittker & Rahdert, _supra_ note 2, at 332.

9. Belknap puts it as follows:

> "[G]overnment has granted the charitable tax exemptions in order to encourage voluntary private organizations to carry out certain activities which by common understanding are agreed to rate among the highest in the scale of social values. The preference that these activities be carried out by voluntary private organizations is based upon two advantages that private action in these fields enjoys over government action.
>
> "The first advantage is that voluntary private enterprise can often do the job better. . . .
>
> "The second advantage of private control . . . lies in the effect of such control upon the overall pattern of our society. . . . [T]he broad ramifications of freedom require a preference for private activity and diversity." Belknap, _supra_ note 2, at 2035-36.

See also Stone, _supra_ note 2, at 39-40.

10. See Bittker & Rahdert, _supra_ note 2, at 332-33:

> "Lacking a method for measuring these appealing but elusive virtues, one must perforce rely on intuition in comparing the achievements of private charities with those of government, when they are performing similar functions."

11. We could require a conjunction of charitably-aimed public benefit _and_ diversity, thus excluding, e.g., General Electric Corp. from the justification. Even so, the theory would not explain why for-profit hospitals, health clubs, and schools are not exempt from the income tax.

12. The rationale may be fairly close to the mark in explaining why, over time, various entities in the not-for-profit sector have been made tax exempt. To the extent that its very "fuzziness" encompasses the variety of our history, it correspondingly fails to be useful as a predictor of any particular issue's outcome in the future.

13. See Bittker & Rahdert, *supra* note 2, at 307-16. For example:

> "[A]ll exempt organizations engaged in public service activities share one common feature: if they were deprived of their exempt status and treated as taxable entities, computing their 'net income' would be a conceptually difficult, if not self-contradictory task." *Id*. at 307 (footnote omitted).

The authors also argue that, even if an appropriate tax base could be defined, it would be difficult to fix an appropriate tax *rate* to apply to it. *Id*. at 314-16.

14. See, e.g., Hansmann, *supra* note 2, at 59-62. In particular, Hansmann finds no problem in using traditional tax-base and tax-rate notions in the case of "commercial" nonprofit organizations:

> "But Bittker and Rahdert overstate the difficulties. To begin with, many nonprofits receive little or no income from donations, but rather derive all or nearly all of their income from sales of goods or services . . . For such organizations it would be perfectly easy and natural to carry over the tax accounting that is applied to business firms . . . ." *Id*. at 59.

Hansmann goes on to argue that Bittker and Rahdert exaggerate the definitional difficulties even in the case of "donative," as opposed to "commercial," nonprofits. *Id*. at 61-62.

15. See Bittker & Rahdert, *supra* note 2, at 314-16. This fourth theory, although listed separately from the third, is closely linked to the latter. Indeed, the authors viewed it as really part of the appropriate-tax-rate issue.

16. See Hansmann, *supra* note 2, at 65.

17. Hansmann, *supra* note 2, at 65, arguing that in such cases the tax burden would not be "especially regressive."

18. See, e.g., Hansmann, *supra* note 2, at 65 n. 41. These issues are outside the scope of this paper, as remarked in note 1, *supra*.

19. Hansmann, *supra* note 2, at 66.

20. Hansmann, *supra* note 2. The adverb derives from personal conversations between the author and Prof. Hansmann.

21. Hansmann, *supra* note 2, at 68. The notion is further explicated, and examples are provided, *id*. at pp. 69-70.

22. *Id*. at 72-75.

23. *Id*. at 75.

24. Consider, for example, the policies behind the adoption of I.R.C. section 4942, captioned "Taxes on failure to distribute income." See generally B. HOPKINS, *supra* note 2, at 526-43.

25. It is not possible to explore all of the reasons in this paper. However: (a) since not *all* industries would be characterized by contract failure, some workable definition of each "industry" would have to be provided; (b) mechanisms would be needed to prevent entities from flowing their excess capital out of intended industries directly or indirectly into other uses and industries; (c) some method would be required for periodic reviews to measure whether the desired capital build-up had been achieved, so that tax exemption could be withdrawn.

26. *New York Trust Co. v. Eisner*, 256 U.S. 345, 349 (1921) (Holmes, J.). Compare his earlier apothegm, "The life of the law has not been logic: it has been experience." O. HOLMES, THE COMMON LAW 1 (Little Brown 1881).

27. G. SANTAYANA, I THE LIFE OF REASON (1905).

28. Plutarch ascribes these words to Heraclitus in CONCERNING THE E AT DELPHI 18, 392B. See also Plato, Cratylus 402A.

29. L. HAND, *On Receiving an Honorary Degree (1939)*, THE SPIRIT OF LIBERTY 104 (Vintage Books 1959).

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THE TWO INDEPENDENT SECTORS

by

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I. INTRODUCTION

By the year 2000 there will be two relatively distinct independent sectors in the United States. The first, which we might call the philanthropic independent sector, will comprise donatively supported organizations such as charities for the relief of the poor and distressed, cultural organizations such as museums and performing arts groups, and institutions dedicated to research and higher education. The second independent sector will comprise the so-called "commercial" nonprofits[1] -- that is, nonprofits that receive virtually all of their income from the sale of services rather than from donations, and that frequently compete directly with for-profit firms. This second independent sector, which we might call the commercial independent sector, will include, for example, most nonprofit hospitals, health maintenance organizations, medical testing labs, nursing homes, health and life insurance companies, day care centers, and fitness centers. This second independent sector scarcely existed in 1900; by the year 2000 it is likely to account for more than two-thirds of the nonprofit sector as a whole.

II. REASONS FOR THE EMERGENCE OF THE SECOND INDEPENDENT SECTOR

In considerable part, the second independent sector has evolved out of the first one. Hospitals provide the most important, conspicuous, and well-analyzed example. Until this century, nonprofit hospitals were philanthropic institutions devoted primarily to the care of the poor, and were dependent upon donations for most of their income. But a series of revolutions in the technology and financing of health care changed that situation radically in recent decades, to the point where now the prosperous as well as the poor use hospitals, and where the overwhelming majority of hospital patients, rich or poor, are able to pay, either directly or through private or public insurance, for the services they receive. Consequently, most nonprofit hospitals today receive virtually no meaningful amount of donative income, and have become purely commercial nonprofits.[2]

Now that the function of providing subsidized care for the poor has largely been taken away from them, nonprofit hospitals are arguably anachronistic, providing no important services that are not provided as well or better by for-profit hospitals. Nevertheless, even after of two decades of strong competition from chains of aggressively expansionist for-profit hospitals, the market share of nonprofit hospitals remains roughly what it was twenty-five years ago, and shows little sign of declining in the future.[3] This strong resilience of the nonprofit hospitals long after their raison d'etre has disappeared is probably due to several factors. First, despite the claims of their detractors,[4] nonprofit firms evidently often operate with considerable efficiency when faced with financial stringency, and hence cannot easily be driven out of business simply through competition from for-profit firms. Second, the capital that's invested in nonprofit firms cannot be withdrawn and invested in other industries without great difficulty; consequently, whether or not that capital is bringing in a market rate of return, it tends to remain locked into the industry. Third, nonprofit hospitals continue to have the advantage of tax exemption and various other public policy preferences, though the available empirical evidence is ambiguous as to whether these subsidies have had a strong effect on their market share.[5] And fourth, administrators and medical staff affiliated with existing nonprofit hospitals probably have a stake in retaining the nonprofit form, which may offer them greater control, financial remuneration, and protection from competition than would for-profit firms.

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[1] See Henry Hansmann, "The Role of Nonprofit Enterprise," 89 Yale Law Journal 835 (1980).

[2] See Hansmann, supra; Gray, Bradford H., The New Health Care for Profit: Doctors and Hospitals in a Competitive Environment (1983).

Not all commercial nonprofits have evolved from philanthropic ones, however. There are some industries in which commercial nonprofits have played an important role in the industry from its inception. One of the clearest and most interesting instances of this, and one of the oldest as well, is consumer savings banking.[6] That industry, when it first took shape at the beginning of the nineteenth century, was initially populated almost exclusively by nonprofit firms, in the form of mutual savings banks. (Despite their name, mutual savings banks, unlike mutual savings and loan associations, are not consumer cooperatives, but rather are true nonprofits with no elements of depositor ownership.) Here the nonprofit form served a fiduciary role toward the bank's depositors, providing important protection for them at a time when stock banks were too risky for ordinary citizens to trust with their life's savings.

In time, however, state and federal regulation, as well as

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3. See Gray, *supra*.

4. E.g., Regina Herzlinger and William Krasker, "Who Profits from Nonprofits?," *Harvard Business Review* 93 (January-February, 1987).

5. See Henry Hansmann, "The Effect of Tax Exemption and Other Factors on the Market Share of Nonprofit Versus For-Profit Firms," 40 *National Tax Journal* 71 (1987).

6. See Eric Rasmussen, "Stock Banks Versus Mutual Banks," *Journal of Law and Economics* (forthcoming); Henry Hansmann, "The Role of Commercial Nonprofits: The Evolution of Savings Banks," in Helmut Anheier and Wolfgang Seibel, eds., *The Nonprofit Sector: International and Comparative Perspectives* (forthcoming).

the increasing maturity of the banking industry itself, endowed stock banks with a degree of trustworthiness comparable to that of nonprofit banks. Indeed, with the adoption of federal deposit insurance in the 1930s,[7] mutual savings banks lost their comparative advantage entirely, and became anachronistic. Yet they have continued to occupy a significant place on the economic scene for another half century, probably for reasons similar to those outlined above in the case of hospitals.

There are many other industries heavily populated with commercial nonprofits that seem to have followed one or the other of these patterns of evolution. Indeed, both patterns may be present in many industries. For example, the commercial nonprofits that are found today in the nursing home industry and the day care industry seem to have evolved in part from firms that originally were established as philanthropic entities, though it also appears that many of these firms were essentially commercial nonprofits from their founding, and presumably adopted the nonprofit form to offer some extra degree of assurance to prospective customers that they would provide quality care.

Now, as I've already suggested, the two industries that I've focused on as examples here, namely hospital care and savings banking, are industries in which commercial nonprofits appear today to serve no functions that cannot be served as well or better by for-profit firms. And arguably the same conclusion could be drawn about commercial nonprofits in other industries, such as health maintenance organizations, health insurance, and medical testing. Yet we cannot safely conclude that commercial nonprofits are always nonfunctional. There may well be some industries in which commercial nonprofits today serve much the same role that they served in the savings bank industry in its early stages, providing a degree of fiduciary protection for customers against opportunistic behavior in an environment where consumers are for some reason in a poor position to police the quality of service that a firm promises or delivers. For example, though there is much debate on the subject, some commercial nonprofits may be serving such a function today in the nursing care and day care industries.[8]

In any event, the tendency of nonprofit firms to become embedded once they are established indicates that, in the absence of any changes in public policy, we are likely to face a constantly growing population of commercial nonprofits in the future, many of which will be anachronistic. Indeed, given the tendency of government to take over many of the functions traditionally performed by charity, philanthropic nonprofits are likely to find their role continually shrinking as the number of commercial nonprofits expands, thus resulting in the continued growth of the second independent sector relative to the first.

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[7] And with the imposition of interest rate controls on banks of all sorts.

[8] See Henry Hansmann, "Economic Theories of Nonprofit Organization," in Walter Powell, ed., The Nonprofit Sector: A Research Handbook (1987).

III. THE RESPONSE OF THE LAW TO THE EMERGENCE OF A DUAL INDEPENDENT SECTOR

Having said something about the reasons for the emergence of the two independent sectors, I would like to survey the way in which public policy has been responding to this development, and the way in which it is likely to respond in the future.

If current trends continue, by the year 2000 the two independent sectors are likely to be strongly distinguished in law as well as in fact.

A. Tax Law

These trends are most conspicuous in the area of taxation. In principle, the federal corporate income tax presumes that all nonprofit corporations are taxable unless they can establish that they fit into one or another specific exemption set out in the Internal Revenue Code. In practice, however, the exemptions have traditionally been read so broadly as to encompass nearly all nonprofits of any financial significance. And the same has largely been true of state property and sales taxes. In effect, nonprofits as a class have been presumed exempt, and only special types of nonprofits have ever been taxed. In general, the words "nonprofit" and "tax-exempt" have been coterminous.

The emergence of the second independent sector has now begun to threaten this regime seriously. Many of the new commercial nonprofits appear so clearly to be providing services that are no different from those offered by for-profit firms that continued tax exemption is conspicuously difficult to rationalize.[9] And in fact Congress has recently taken strong action in this regard, withdrawing tax exemption in 1986 from nonprofit organizations "providing commercial-type insurance"[10] -- which has been interpreted to include, for example, Blue Cross/Blue Shield and TIAA/CREF. There is good reason to believe that this is simply the beginning of an assault on the exemption for many types of commercial nonprofits. At least one Congressman has already

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9. See Henry Hansmann, "The Rationale for Exempting Nonprofit Organizations from the Corporate Income Tax," 91 Yale Law Journal 54 (1981).

10. I.R.C. sec. 501(m).

proposed withdrawing tax exemption from nonprofit hospitals,[11] for example, and I suspect that that exemption will soon come under much broader attack. Federal corporate tax exemption for most or all of what I have called the second independent sector may soon be in doubt. And the same applies to state and local taxes, including not just state corporate income taxes but also property and sales taxes. Indeed, some states have already begun to restrict exemption for hospitals,[12] fitness centers,[13] and other types of commercial nonprofits.

As a result of this development, serious thought will have to be given in the years ahead to defining the appropriate scope for tax exemption. Should all commercial nonprofits be denied exemption, thus in effect extending the exemption only to donative nonprofits? Or should some commercial nonprofits still be exempt? And if so, which ones? Should the tax code try to track the distinction, suggested above, between commercial nonprofits that are anachronistic and those that continue to perform a role that distinguishes them from for-profit firms? Would such a distinction be administrable -- for example, in the form of a commerciality test of some type? Does it make most sense for the legislature to proceed on an industry-by-industry basis here, as it has in the case of insurance?[14]

Note, moreover, that many of the new commercial nonprofits continue to obtain their exemption under the general exemption granted "charities." For example, the nonprofit insurance companies from which Congress recently withdrew exemption had previously been exempted as charities. Thus the refashioning of tax law to deal with the second independent sector is going to force legal scholars and lawmakers to think more seriously about what is meant by the concept of charity -- a task that is about four hundred years overdue.

Wherever the line is ultimately drawn between exempt and nonexempt nonprofits, in the end there's likely to be a large portion of the nonprofit sector that's nonexempt -- indeed, perhaps the great bulk of the sector will be nonexempt. And if this happens, the distinction between exempt and nonexempt organizations will come to be a highly visible line of demarcation between the two independent sectors.

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[11] Scott Jaschik, "Congressman Advocates End to Tax Exemption for Non-Profit Hospitals," *Chronicle of Higher Education* 1 (July 22, 1987).

[12] Utah County v. Intermountain Health Care, Inc., 709 P.2d 265 (Utah 1985).

[13] Nancy Davis, "The Competition Complex," *Association Management* 24 (August 1986).

[14] See generally Hansmann, *supra* note 9.

What would happen to the size and scope of the second independent sector if tax exemption were withdrawn from it? It is hard to say. On the one hand, the existing empirical work suggests that the market share of nonprofit versus for-profit firms is relatively sensitive to tax exemption.[15] On the other hand, experience with non-profit-seeking firms in other sectors, such as mutual insurance companies, suggests that once such firms are well established, the absence of tax exemption or other perquisites does not inhibit their ability to maintain their share of the market.[16] It is quite possible that the nonprofit hospitals, nursing homes, day care centers, health maintenance organizations, home health care agencies, and other institutions that populate the second independent sector will come to appear to us much as mutual insurance companies do now -- that is, as essentially commercial entities that do not much differ from their for-profit competitors, and that are not treated much differently by public policy.

B. Other Forms of Special Treatment

Even if, as I've predicted, tax exemption is ultimately withdrawn from most or all of the second independent sector, the donatively-supported nonprofits that make up the first independent sector seem likely to retain their exemption (and probably the charitable deduction as well). But a different pattern is emerging in other areas of the law where nonprofits have heretofore received special treatment. In a number of these areas the response to the rise of the second independent sector has been not just to withdraw preferential treatment from the commercial nonprofits that constitute that sector, but from all nonprofits. Labor law is an example. Prior to 1970, virtually all nonprofit organizations were exempted from federal labor law. Then, beginning in that year, the National Labor Relations Board used its discretion to withdraw this exemption from selected nonprofits.[17] A critical step in this process was Congress' decision, in 1973, to pass legislation specifically withdrawing labor law exemption from nonprofit hospitals[18] -- a decision presumably based on the increasingly commercial character of nonprofit hospitals. Yet the process did not stop there, and by 1976 the NLRB had proceeded to withdraw exemption from all nonprofits, including even small charities supported entirely by donations.[19]

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[15] See Hansmann, supra note 5.

[16] See Henry Hansmann, "The Organization of Insurance Companies: Mutual Versus Stock," 1 Journal of Law, Economics, and Organization 125 (1985).

[17] Cornell University, 183 N.L.R.B. 329 (1970).

[18] Public Law 93-360 (July 16, 1974), amending sec. 2(2) of the National Labor Relations Act.

Moreover, a similar process seems underway in other areas, from antitrust law[20] to subsidized postal rates.[21] Thus the rise of the second independent sector is threatening the privileges of the traditional philanthropies as well.

C. Corporate Law

Nonprofit corporation law has also been struggling to come to grips with the emergence of two distinct independent sectors. In particular, the American Law Institute has recently released a proposed Model Nonprofit Corporation Act, which is being proposed for enactment by states throughout the country. In contrast to most existing nonprofit corporation statutes, this Act formally splits all non-religious nonprofits into two different categories. Traditional charities are to be governed by the first of these categories, while social clubs and other membership organizations are to be governed by the second. Just where most commercial nonprofits are to go in this scheme is presently quite unclear. But there are indications that many of them are intended to be put in the second category, thus creating a further division between the two independent sectors.[22]

IV. MIXED CASES

So far I've been speaking of a growing divergence between two different types of nonprofit organizations. But much the same development is of course also occurring within individual nonprofit organizations. Without giving up their reliance on donative support, many philanthropic organizations in what I have called the first independent sector are engaging in increasing amounts of commercial activity to increase their income. It is commonly said that the reason for this is that nonprofits have recently become hard pressed by cutbacks in public and private contributions. I find this explanation quite unpersuasive. It would seem to follow from this explanation, for example, that the commercial activity of nonprofits should have been most extensive not now, but rather earlier in the century, when the need for the charitable services and public goods provided by nonprofits were

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19. The process was essentially completed in St. Aloysius Home, 224 N.L.R.B. 1344 (1976).

20. See N.C.A.A. v. Board of Regents, 104 S.Ct. 2948 (1984).

21. 39 U.S.C.A. sec. 3626.

22. For a detailed critique of the California Nonprofit Corporation Act, on which the proposed Model Act is very closely modeled, see Henry Hansmann, "Reforming Nonprofit Corporation Law," 129 University of Pennsylvania Law Review 129 (1981).

far greater, and the sources of private and public support for the nonprofit sector were much smaller. Rather, I think that the expanding commercial activity of otherwise charitable nonprofits grows out of much the same conditions that have given rise to the growth of the second independent sector in general, and if anything reflects a decreasing need today for the types of services that can only be provided by nonprofit organizations.

In any event, the same problems that are arising between the two independent sectors are also appearing within individual organizations. Thus, to take one conspicuous example, the taxation of unrelated business income has recently become a very lively topic of debate.[23]

V. IMPLICATIONS FOR THE MANAGEMENT OF NONPROFITS

As a consequence of the emergence of the second independent sector, managers of nonprofit organizations are now faced with large and difficult questions about the purposes their organizations are to serve. Managers of the new commercial nonprofits, in particular, must constantly ask themselves whether, and why, the fact that they are nonprofit affects what their organization is doing -- and, most importantly, how it affects what their organization should be doing. Should a nonprofit hospital try hard to provide services that are somehow different from those offered by a for-profit hospital? Should the YMCA's fitness centers offer services that are clearly different from those offered by for-profit fitness centers? If so, just how should their services be different? If not, why are they nonprofit, much less tax-exempt? In short, organizations within the second independent sector are faced with a massive identity crisis, and the managers of these institutions are somehow going to have to deal with it. Moreover, a minor identity crisis of this sort affects even the managers of traditional philanthropies every time they decide whether to undertake a new commercial venture.

VI. A DIVERGENCE OF INTERESTS BETWEEN THE TWO INDEPENDENT SECTORS

The emergence of two distinct independent sectors also creates a dilemma for organizations like Independent Sector that seek to represent the interests of the nonprofit sector as a whole. For, as we approach the year 2000, the interests of the two independent sectors may increasingly diverge.

For example, rather than fighting to retain special subsidies and preferences, such as tax exemption, for all nonprofits, it may

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23. See Hearings on the Unrelated Business Income Tax, Subcommittee on Oversight of the Committee on Ways and Means, U.S. House of Representatives, June 1987.

be in the interest of the first independent sector -- the philanthropic nonprofits -- to protect themselves by, as it were, throwing the second independent sector to the wolves. More particularly, the traditional philanthropies may wish to lobby for the creation of a clear line between those nonprofits that will continue to benefit from special preferences, such as tax exemption, and those that will not, and to place the second independent sector on the far side of the line. The alternative could be that ultimately preferences will be lost for all nonprofits, including the philanthropic ones. In short, it may be rational for the philanthropic independent sector to conclude that, if united we stand, then united we will fall. And similar conflicts of interest are likely to arise in other areas of law and policy as well.[24]

VII. CONCLUSION

The very forces that have caused the nonprofit sector to grow so rapidly in recent decades have also led to important shifts in the composition of that sector. Those changes are likely to continue between now and the year 2000, leaving us then with an even more diverse -- and divided -- set of organizations than we have now. As a consequence, there will be difficult questions of policy to be addressed in the years to come, both for lawmakers and for leaders within the nonprofit sector itself.

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[24] A divergence of interests between the two independent sectors is also likely to emerge in corporation law, though here it will take a slightly different form. While it will be in the interest of many commercial nonprofits to be governed by the relatively permissive Mutual Benefit provisions of the Model Nonprofit Corporation Act, it may be in the interest of the philanthropic nonprofits to have them governed by the more stringent Public Benefit provisions in order to reduce the possibility for opportunism and fraud on the part of the commercial nonprofits that might tarnish the public image, and detract from the public support, of the nonprofit sector as a whole.

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BUDGET NEUTRAL OPTIONS TO ENCOURAGE CHARITABLE GIVING

by

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Prepared for the 1988 Spring Research Forum
"Looking Forward to the Year 2000:
Public Policy and Philanthropy"

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BUDGET NEUTRAL OPTIONS TO ENCOURAGE CHARITABLE GIVING

Lawrence B. Lindsey

The 1980s have proved to be the worst decade on record for providing tax incentives to promote charitable giving. Numerous changes in the tax law, principally in the Economic Recovery Tax Act of 1981 and the Tax Reform Act of 1986, have sharply reduced the incentives for taxpayers to make charitable gifts. In addition, the federal budget situation has created both an increased need for charitable giving and decreased scope for providing charitable incentives.

This paper considers alternatives to the present tax treatment of charitable giving which are designed to increase incentives for giving without decreasing tax revenue. The first section briefly reviews the changes which have been made in the 1980s which reduced incentives for charitable giving. The second section provides the budgetary case for revenue neutral changes in the tax treatment of donations. In the third section, various revenue neutral options are presented with separate estimates of the cost of various incentives and the ways to pay for those incentives.

I. The Declining Incentives for Charitable Giving

Tax incentives for charitable giving are as old as the income tax. Shortly after its enactment in 1913, it was acknowledged that charitable gifts should not be part of the income tax base as the money involved did not benefit the donor, but the charitable recipient. As the ultimate recipient was not subject to tax, it was decided that no tax should be levied on income which was contributed to charity. Charitable gifts thus became an early adjustment to income, lowering the taxpayer's income which was subject to tax.

Recent analysis of charitable giving by the "tax expenditure" approach has neglected this original, and ultimate, justification for excluding charitable giving from the tax base. Presently, a majority of American taxpayers are denied any deduction for their charitable gifts. Equally important, the amount of "tax expenditure" on charitable giving was sharply curtailed during the 1980s, from 11.3 billion in 1981, or 0.45 percent of personal income to an estimated 9.0 billion in 1988, a mere 0.23 percent of personal income, or half the level of 7 years earlier. This decline in the tax expenditure budget for charitable giving sharply increased the after-tax cost of making a charitable donation, which is the relevant measure of incentive from the point of view of the donor.

Much of the rise in the cost of charitable giving has little to do with direct legislative action regarding charitable giving. Rather, it is the result of changes in other provisions of the tax law which have an indirect effect on the after-tax cost of making a charitable gift. Most notable is the sharp reduction in marginal tax rates during the 1980s. In 1981, the average marginal tax rate facing itemizers was 29.5 percent, and under old law would have risen to 30.7 percent in 1984 and 34.1 percent in 1988. The Economic Recovery Tax Act of 1984 cut this rate to 23.7 percent in 1984 and the Tax Reform Act of 1986 cut the 1988 marginal rate to an estimated 21.3 percent.

The price, or after-tax cost of making a charitable gift is the change in the donor's after-tax income as a result of making the gift. For example, if someone makes a gift of $1 and is in the 20 percent tax bracket, his taxes go down 20 cents, producing a net price of 80 cents. As a result of these rate reductions, the after-tax cost of making an additional contribution of $1 for the typical itemizer was increased from 69.3 cents to 76.3 cents in 1984 and from 65.9 cents to 78.7 cents in 1988.

The second major change in the tax law during the 1980s was a change in the number of taxpayers eligible for a tax incentive for their charitable gifts. In most cases, taxpayers were required to itemize their charitable deductions in order to receive an incentive to make a contribution. The number of taxpayers eligible for such treatment depends upon what other itemized deductions are allowed, and the level of the threshold for itemizing, called the standard deduction or zero bracket amount.

The Economic Recovery Tax Act of 1981 was quite beneficial to charities with respect to eligibility. First, ERTA maintained the zero bracket amount at the same nominal level as the year of enactment. Due to inflation and real economic growth, the percent of taxpayers with deductions over this threshold rose steadily, from 33.1 percent in 1981 to 39.2 percent in 1986. Thus, increasing numbers of taxpayers were eligible for the deduction.

ERTA also extended the deduction of charitable gifts to non-itemizers in a gradual way. During the period 1982-1984, taxpayers were allowed to deduct a share of gifts up to a ceiling amount. By 1985, the ceiling was removed, and in 1986, full deductibility of all charitable gifts was allowed for all taxpayers. Although the extension of full deductibility was a major positive step in the tax code, the intermediate year provisions were poorly designed to promote charitable giving The vast majority of all gifts by non-itemizers are given by taxpayers who gave more than the ceiling amounts in place during

1982-1984. Thus, no marginal incentive for extra giving was provided to the donors of the vast majority of all gifts. Nonetheless, the inframarginal incentive of partial deductibility cost the Treasury money. Opponents of charitable giving incentives point to these years to make a case against more generous treatment of charitable giving. In fact, very little extra incentive to give was provided during these years. The poor design of the charitable giving incentive was the reason for its ineffective results.

The Tax Reform Act of 1986 reversed the extension of charitable giving incentives to non-itemizers and sharply curtailed the number of itemizers. As Table 1 shows, the number of taxpayers enjoying a charitable incentive fell dramatically as a result of the 1986 Act.

Table 1

Effect of New Tax Bill on Itemizer Status

(1) New AGI Class	(2) Number of Taxpayers	(3) Stay Itemizers	(4) Become Non-itemizers	(5) Remain Non-itemizers
0-10	27.9	1%	1%	98%
10-20	25.1	7%	13%	80%
20-30	19.4	20%	29%	51%
30-40	14.5	41%	33%	26%
40-50	9.5	61%	24%	15%
50-75	9.2	74%	16%	10%
75-100	2.3	82%	8%	10%
100-200	1.8	86%	6%	8%
over 200	0.6	91%	3%	6%
TOTAL	110.7	26%	16%	58%

AGI Classes in Thousands
Number of Taxpayers in Millions
All figures for 1988

The new law removed the charitable incentive for non-itemizers. This eliminated 58 percent of the taxpayer population (Column 5) from the benefits of the old law. In addition, by narrowing the scope of other deductions, and by raising the standard deduction, the new law caused some 16 percent of taxpayers (Column 4) to switch from being itemizers to being non-itemizers. These "switchers" are particularly important in the key $20,000 - $50,000 income group where they comprise between a quarter and a third of all taxpayers. The overall effect of the new law was to limit the tax incentive for charitable giving to only about one quarter of all taxpayers

A third major change in the 1986 tax law was the inclusion of the appreciated portion of gifts of property in the minimum tax base. This decision had the effect of raising the price of giving to high income donors who make large contributions. In 1988, some 70,000 taxpayers with incomes over $200,000 will be subject to the minimum tax. These taxpayers will face a price of 79 cents on both their gifts of cash and their gifts of property. Although they comprise only about 12 percent of taxpayers earning over $200,000, these minimum taxpayers contribute more than 40 percent of the $7.4 billion given by upper income taxpayers, or more than $3 billion.

The impact of the of minimum tax on the price of giving by high income taxpayers is therefore quite dramatic. Some 10.4 cents of a total 25 cent increase in the price of giving by upper income taxpayers is due to the price increase faced by taxpayers in the minimum tax. The overwhelming majority of the value of the gifts by these taxpayers are large (over $100,000) contributions of appreciated assets. Groups which rely on these gifts are likely to face a particularly difficult situation.

The combined effect of these provisions is a dramatic increase in the price of making a charitable gift. Table 2 presents the overall effect of the 1986 bill on charitable giving.

Table 2

Weighted Average Price of Charitable Giving

New AGI	Itemizers-New Law		All Taxpayers	
Class	Old Law	New Law	Old Law	New Law
0-10	.965	.950	.920	.987
10-20	.850	.879	.847	.977
20-30	.793	.815	.800	.931
30-40	.748	.806	.750	.889
40-50	.716	.765	.714	.828
50-75	.656	.707	.655	.753
75-100	.591	.702	.596	.736
100-200	.536	.686	.538	.702
over 200	.448	.696	.450	.700
Total	.657	.748	.718	.854

AGI classes in thousands
All figures for 1988

The table shows that, weighted by gifts, the price of charitable giving will rise from about 72 cents on the dollar to more than 85 cents. Stated differently, nearly half the 28 cent "tax expenditure" made per dollar of charitable giving was eliminated by the 1986 tax law changes.

II. The Budgetary Effects of Tax Incentives for Giving

While the effect of tax changes during the 1980s was to sharply cut the tax incentives to make charitable contributions, an enormous amount of econometric evidence suggests that generous incentives for charitable giving make sound budget policy. The effect of a tax incentive for charitable giving is to lower the price of making the gift. At lower prices, donors tend to buy more of the good in question -- in this case, give more to charity. The amount of responsiveness to a lower price is known as the "price elasticity" which shows the percent increase in charitable giving for every one percent decrease in the price of making a gift. Clotfelter (1985) provides an outstanding review of this literature, which is also summarized in Lindsey (1987). The evidence is overwhelming that a one percent cut in the price of giving will increase giving by more than one percent.

The price elasticity of charitable giving is important for budget policy as well. The price elasticity also happens to be the ratio of the increase in donations to the number of incremental dollars spent as a "tax expenditure" to lower the marginal cost of giving. Since the price elasticity is a number greater than one, each dollar expended by the federal government on increased incentives for charitable giving will increase charitable giving by more than one dollar. There are very few avenues of government expenditure that do more than one dollar's worth of good for every one dollar expended.

In fact, careful design of the charitable giving incentive can increase the ratio of charitable gain per dollar expended. Feldstein and Lindsey (1983) showed that the appropriate use of floors on charitable giving deductions for non-itemizers can increase the budgetary efficiency of such provisions by up to 50 percent. A floor on the charitable giving provision means that donors receive a full incentive to make incremental contributions, but do not receive a tax reduction for contributions they were likely to make anyway. This makes it possible to use each government dollar as efficiently as possible in increasing the total amount of charitable donations.

There are two principal ways that government can increase incentives for individuals to make charitable contributions. The first is to increase the incentives for those donors who already receive some tax incentive, namely itemizers. Such an incentive could take the form of an "add-on" credit or of a "multiple deduction". In the case of the add-on credit, each taxpayer could take an itemized deduction as under current law, but would also be allowed a tax credit against his tax liability for every dollar donated. For example, a 10 percent add-on credit would lower the price of giving for someone in the 28 percent bracket from 72 cents on the dollar to 62 cents. The credit could be extended to all contributions, or, to increase the budgetary efficiency of the plan, only those contributions above a particular floor. In contrast, a multiple deduction would allow the taxpayer to deduct more than the cost of the gift. A 150 percent deduction, for example, would permit someone who gave $100 to take a tax deduction of $150. For someone in the 28 percent tax bracket, the effective price of giving would be reduced from 72 cents on the dollar to 58 cents on the dollar. As in the case of the add-on credit, the multiple deduction could be taken either for all donations, or for donations above a certain floor.

The budgetary efficiency of either an add-on credit or a multiple deduction would be roughly equal to the price elasticity of charitable giving. That is, for every dollar the government expends on increasing the incentive for giving, charities will gain more than one dollar. The imposition of a floor on the incremental incentive has two effects. First, it lowers the revenue cost of the incentive for each taxpayer who gives at least as much as the floor. The amount of revenue saved is the taxpayer's marginal tax rate times the dollar amount of the floor. Second, the floor eliminates the incremental incentive to contribute for all taxpayers who give less than the floor. This second effect lowers the incremental amount of giving induced by the incentive.

The budgetary efficiency of imposing the floor depends on the offsetting effects of these two factors. At low levels, the floor affects the incentives of few taxpayers and only a small share of the amount contributed. On the other hand, the floor lowers the revenue cost of the incentive for a great many taxpayers. This means a large overall savings. Thus, a low level floor will greatly enhance the budgetary efficiency of an incremental incentive. However, as the floor rises, fewer taxpayers are eligible for the incentive, thus decreasing the effect of the incentive on contributions. Furthermore, as the floor rises, the incremental revenue gain will tend to decrease The actual budgetary efficiency of a floor depends on the distribution of charitable donations among the population receiving the incentive.

The provision of an add-on credit or multiple deduction to itemizers is unlikely to occur politically. The reasons for this are largely distributional. As upper income taxpayers tend to be more likely to be itemizers than lower income taxpayers, and as contributions tend to rise with income, most of the tax incentive from such provisions would accrue to taxpayers at the top of the income distribution. In addition, it may seem inappropriate to give an additional incentive to the quarter of taxpayers who itemize while three quarters of all taxpayers receive no incentive at all. Therefore, the focus of the analysis must turn to providing incentives to contribute to the non-itemizing population.

The budgetary analysis of incentives for charitable giving for non-itemizers is similar to that for itemizers. Absent a floor, the budgetary efficiency of such a provision is approximately equal to the price elasticity of demand for charitable giving. With a floor, the budgetary efficiency depends on the distribution of giving among the population receiving an incentive. Table 3 shows the distribution of giving among the non-itemizing population.

Table 3

Level of Donation	Percent of Non-itemizers	Percent of Non-itemizer Giving
Zero	52.1	0.0
Under $50	6.9	1.0
$50 - $100	5.7	2.2
$100 - $150	5.7	3.7
$150 - $200	4.5	4.1
$200 - $250	3.3	3.9
$250 - $300	2.7	3.9
$300 - $400	3.9	7.1
$400 - $500	3.1	7.1
over $500	12.0	66.9

The table shows that the distribution of donors by level of donation is quite different from the distribution of total donations by level of donation. On the one hand, the vast majority of all non-itemizers, 64.7 percent, reported gifts of less than $100 on their tax return. Although this group comprised the vast majority of donors, their total giving amounted to only 3.2 percent of the total amount contributed by non-itemizers. On the other hand, only 12 percent of non-itemizers contributed over $500, but their gifts comprised two thirds of non-itemizer giving.

This clearly shows that a tradeoff exists when a floor is considered. A high floor permits a generous incentive for those donors who contribute the vast majority of all gifts. On the other hand, such a floor would exclude the vast majority of all donors from receiving any incentive. Imposition of a floor on non-itemizer giving presents a sharp trade-off between the universality of an incentive and its generosity.

There is one important difference in the analysis of the budgetary efficiency of an incentive for non-itemizers and an additional incentive for itemizers. Provision of a charitable incentive for non-itemizers may cause itemizers to change their tax status. This results in a loss of revenue for the government without increasing the incentive for the taxpayer to contribute. Consider the following example. The standard deduction is $5000. A taxpayer has charitable contributions of

$3000 and other deductions of $3000. If there is no charitable deduction for non-itemizers, then this taxpayer chooses itemizer status as his total deductions of $6000 exceed the $5000 standard deduction. However, if there is a charitable deduction for non-itemizers, then it is in this taxpayer's interest to become a non-itemizer. In that case, the taxpayer would be entitled to the $5000 standard deduction and the $3000 charitable deduction, for a total deduction of $8000. By contrast, staying an itemizer would have provided this taxpayer with only $6000 in total deductions.

Taxpayers in this situation, known as "switchers" because they switch itemizer status, lower the budgetary efficiency of providing charitable incentives for non-itemizers. Each dollar expended providing an incentive for non-itemizers to contribute will therefore bring in fewer dollars to charity than dollars expended to increase the incentive for itemizers to contribute. Nonetheless, distributional considerations make providing an incentive for non-itemizers more likely than increasing the incentives for itemizers. In either case, the increased giving to charitable organizations is likely to be greater than the revenue cost to the government of providing the incentive.

III. Making Charitable Incentives Budget Neutral

Although charitable incentives are budgetary efficient in that the gains to charities are more than the costs to the government, a decline in government revenue is still involved. Given the current budget situation, with large deficits, provisions which cause those deficits to widen are likely to be politically difficult. Therefore, particular attention should be paid to proposals which include a way to "pay" for the charitable incentive. It should be made clear that even if the entire cost of the charitable incentive is borne by funds currently received by the charitable community, charities are still made better off on net because of the budgetary efficiency of charitable incentive programs.

There are three ways to provide funds for a charitable incentive program. The first is in the form of direct spending cuts on payments to support charitable activities. Many social services, including higher education, medical research, and community programs, are jointly provided by the government and private philanthropic efforts. Reductions in direct federal spending in these areas, coupled with an earmarking of funds to support additional incentives for contributions to these areas, would increase the total level of funds supporting these social services without increasing the budget deficit. It is likely that any such budgetary program would have to be targetted to a particular area of government spending in order to assure that funds cut from that area would not be reallocated to support other types of philanthropic endeavor.

The second way to "pay" for increasing charitable incentives for some taxpayers is by decreasing the charitable incentive for other taxpayers. In particular, the charitable deduction could be extended to non-itemizers coupled with a floor on the deductibility of charitable gifts by both itemizers and non-itemizers. Table 4 shows the budgeary and giving tradeoffs involved in such a proposal.

Table 4

Effect of a Floor on Charitable Giving

Level of	Change in Taxes			Change in Giving		
Floor	Itemizers	Non-Item	Total	Itemizers	Non-Item	Total
$200	+0.07	-2.25	-2.18	-0.23	+3.66	+3.43
$300	+0.58	-1.90	-1.32	-0.34	+3.35	+3.01
$400	+1.04	-1.64	-0.60	-0.52	+3.08	+2.56
$500	+1.46	-1.41	+0.05	-0.72	+2.78	+2.06

The table shows clearly that only a floor of about $500 on both itemizers and non-itemizers will achieve a revenue neutral result. The need for a high floor is the result of the new tax law, as under old law revenue neutrality could be obtained with a floor of around $200. The reason that the new tax law raised the breakeven threshold is that the new standard deduction is quite high -- $5000 for a married couple. As already noted, this means that there are fewer itemizers. As imposing the floor on itemizers is the revenue producing part of this approach, less revenue is raised.

Compounding this problem is the fact that the high standard deduction produces a very large number of "switchers". Recall that these switchers receive a tax break but do not get any increase in their incentive to give. Under the new law, an estimated 4,910,000 will switch from itemizer to non-itemizer status. Their total giving amounts to $13.1 billion, or roughly 30 percent of total giving by itemizers. The revenue lost due to this switching is roughly $1.2 billion.

The effect of a $500 floor would be to exclude a large number of both itemizers and non-itemizers from receiving a charitable deduction. As the above table indicated, only 12 percent of non-itemizers gave more than $500, although their gifts comprised two thirds of total non-itemizer giving. Only 55 percent of itemizers give more than $500, although their gifts comprise over 95 percent of all itemizer giving. A $500 floor would limit the charitable incentive to the quarter of the population who give more than that figure.

The third method of paying for extending the charitable contribution to non-itemizers is to lower the standard deduction. The justification for this is that a portion of the standard deduction is intended to represent a "standard" level of charitable contributions. Thus, extending the deduction to non-itemizers would make up for the reduction in the level of the standard deduction. Table 5 shows the effect of this proposal on taxes and giving.

Table 5

Effect of a Lower Standard Deduction on Charitable Giving

Reduction	Change in Taxes			Change in Giving		
of S.D.	Itemizers	Non-Item	Total	Itemizers	Non-Item	Total
$200	-0.93	-1.27	-2.20	-0.14	+4.11	+3.97
$300	-0.86	-0.30	-1.16	-0.12	+4.14	+4.02
$400	-0.79	+0.67	-0.13	-0.12	+4.16	+4.04
$500	-0.73	+1.65	+0.92	-0.12	+4.18	+4.06

These numbers indicate that a revenue neutral proposal would involve extension of the charitable deduction to non-itemizers coupled with a $400 reduction in the zero bracket amount. It should be noted that there still is a "switcher" effect from this proposal, although it is smaller. The taxes paid by itemizers fall, due to the switcher effect, while non-itemizers pay more because of the lower zero bracket amount.

It should be noted that this approach has two major advantages over the imposition of a floor on the giving by itemizers and non-itemizers. The first advantage is that it is universal. All donors will be eligible for a charitable deduction under the lower standard deduction approach, in contrast to only about a quarter of all taxpayers under the floor approach. The second advantage is the gain in charitable giving. The net increase in giving is roughly $4 billion under the lower standard deduction, but only about $2 billion under the floor approach. Of course, these effects are inter-related. These results seem to indicate that a reduction in the standard deduction offers the best method of obtaining an increase in the level of giving without causing adverse effects on tax revenue.

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SECTION TWO:

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WORKING DRAFT

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FADING DISTINCTIONS AMONG THE THREE SECTORS: IMPLICATIONS FOR PUBLIC POLICY

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FADING DISTINCTIONS AMONG THE THREE SECTORS:
IMPLICATIONS FOR PUBLIC POLICY

The voluntary nonprofit sector has traditionally played roles distinct from those of the public and the for-profit sectors.[1] As a consequence, the government has adopted public policies favorable to the nonprofit sector. The primary benefit of such policies accrues from the favorable tax treatment conferred upon the nonprofit sector, i.e., the tax exempt status of the organization and the tax deductibility to donors of charitable contributions made to nonprofit organizations. Fostering the nonprofit sector and its unique contributions is not without cost. This preferential treatment at the federal level alone is estimated to entail a tax expenditure, i.e., a cost to the government in terms of lost tax revenues, of 12 billion dollars (OMB, 1987).

There has been considerable attention given in recent years to changes in the nonprofit sector, particularly increased government dependency and commercialization. As nonprofits increasingly resort to the traditional revenue sources of the public sector, i.e., grants, and the for-profit sector, i.e., fees for services, they tend to mirror them. These changes are perceived to have muted the distinctive roles of the nonprofit sector, at least in some industries. If the difference between the behavior of nonprofit organizations and either the public or for-profit sectors has indeed faded, the wisdom of public policies designed to support the nonprofit sector comes into question.

To assess public policy toward nonprofits requires an examination of the extent to which the distinctive roles of the nonprofit sector have eroded, the extent to which current policies are predicated on such roles, and an evaluation of the possibilities for designing public policies to stimulate those roles, i.e., policies based on behavior rather than legal definitions of nonprofit status. This paper begins to address these questions. First, we discuss the nature of the public, nonprofit and proprietary sectors. Second, we consider the extent to which financing affects sectoral distinctions. Two industries, hospitals and higher education, are used as illustrations. Finally, we consider the rationale for and implications of current policies and possible policy changes. In order to make this task more manageable, we limit our discussion to public charities— nonprofit organizations which deliver services that are socially desirable, i.e., provide collective benefits.[2]

Public, Nonprofit, and For-profit Organizational Behavior

Although the activities of the three sectors have never been mutually exclusive, historically they have been quite distinct. Their behavior largely reflects the missions assigned to them and the corresponding economic, legal and political constraints within which they operate.

Proprietary organizations form to produce goods and services and make them available to consumers for a price. For-profit firms respond to the preferences of consumers as reflected in their willingness to pay for services. Property rights to the profits, i.e., the residual between the price which consumers pay for the product and the production costs, possessed by owners provide the incentive for undertaking such activity. For goods and services which are excludable and rival in consumption, such arrangements are efficient.

However, goods and services which are nonexcludable or nonrival in consumption are not efficiently handled by the for-profit sector. Nonexcludability makes it difficult for suppliers to exact a price from consumers. Nonrivalness permits the revealed preferences of consumers to understate the true benefits to society. If either condition exists, the delivery of such services via the for-profit sector will result in an inefficient resource allocation, i.e., an undersupply. Consequently, the responsibility for the delivery of such goods and services should not be left to the market. There is also a need to augment the workings of the market when society decides that access to the market for particular goods and services, e.g., education and health care, is limited for those with low incomes.

Whether markets fail to deliver the efficient output level or "unduly" limit access, decisions about the supply of these goods and services require collective action. Most discussions focus on the government sector as the primary vehicle for collective action. Society's preferences for such goods and services can be voiced through political processes. Once the level of output is chosen, government can then use its power to raise revenues to finance the goods and services and arrange for their delivery.

Of course, collective action does not necessarily translate into government action. The voluntary nonprofit sector is an alternative. Throughout time, especially in American society, there has been a strong reliance on voluntary action to meet collective interests. Voluntary organizations are an effective vehicle for pooling resources to make available goods and services that would not otherwise be supplied. Individuals, on their own volition, can act collectively to provide such goods and services. In fact, as Weisbrod (1977) notes, provision of goods and services by voluntary organizations often predates governmental provision. As an increasingly large number of individuals value the good or service, government reacting to their demands often assumes the responsibility for the delivery of the service. In addition, if such government action fails to fully satisfy the demands of some individuals, it is possible for them to augment government provision via voluntary nonprofit organizations.

Explaining the behavior of nonprofit organizations is much more difficult than explaining the behavior of public or proprietary organizations. This stems from the fact that the nonprofit sector is more heterogeneous.[3] The common thread among nonprofit organizations is their acceptance of the nondistribution constraint, not a specific objective function. As such there are numerous models that have been developed to reflect various characteristics of nonprofit organizations. Models focusing on output maximization, donations, quality, principal-agent problems, and cross-subsidization have been summarized by James and Rose-Ackerman (1986). Based on their review, they conclude that under certain conditions nonprofit managers enjoy greater discretion than their counterparts in the for-profit sector. This expanded discretion results from donations not tied to specific outputs and from barriers to nonprofit sector entry. Nonprofit managers can use their discretion to influence the selection of inputs and choice of outputs. This conclusion is consistent with the theories of nonprofit organizations which suggest that managers self-select into the nonprofit sector because of their strong preferences about product quantity and quality as opposed to monetary rewards (Young, 1986).

Governmental acceptance of the responsibility for service delivery does not obviate the motivations for nonprofit organizations. A distinctive feature of the nonprofit sector is ideology. Many nonprofits are not simply interested in the delivery of a certain quantity of a service, but rather in the quality of the service. These preferences are often based on deeply-held beliefs. For example, James (1987) argues that a primary motivation for the development of the nonprofit educational sector in different societies is the interest in imparting a religious education. This suggests that nonprofit educational sectors characterize countries with a greater degree of religious entrepreneurship. Her empirical analysis both within countries and across countries supports the proposition. As long as preferences with respect to product quality are heterogeneous, nonprofit organizations are a mechanism for responding to those preferences. In effect, the nonprofit sector provides diversity which allows individual choice, in contrast to public production which typically delivers a uniform service.

Government has long recognized the value of such activity by conferring special tax benefits on nonprofit organizations. If the organization wishes, it can apply for such status. But, in exchange, it must accept certain constraints. Although the organization may accrue profits, it is prohibited from distributing the profits. A corollary to the nondistribution constraint, is the reasonable compensation constraint. In effect, officers and managers of the voluntary organization cannot be compensated above reasonable levels. This is intended to prevent the distribution of residuals through compensation premiums.

Funding and the Behavior of Nonprofit Organizations

Given the distinctive missions and the legal constraints within which the sectors operate, the economic base for proprietary, nonprofit and public organizations is quite different. Public bureaus rely almost exclusively on revenues provided from their enabling governments or grants from other governmental entities. The main source of revenues for proprietary organizations are consumer purchases. Consumers are typically individuals, but they may also include governments, e.g., service contracting. Nonprofit organizations have traditionally relied on donations as a primary source of revenue, although they have also charged fees for services as well as received government grants, especially in more recent times.[4] This diversification of revenues is a potential source of the fading distinctions between the nonprofit sector and government or business.

Despite the nonprofit sector's continued use of donations of money and time, there appears to be an increasing reliance on governmental grants and fees for services. The precise cause of this change is uncertain, but it seems reasonable to speculate that it is based on the desire of nonprofit organizations to ensure their survival by diversifying their financial base. Revenue diversification reduces the threat to organizational survival in the event that charitable contributions decline. Moreover, it enables the organization to expand its constituencies, thereby increasing political support.

Revenue diversification by nonprofit organizations can be expected to produce changes in their behavior. In order to secure the resources necessary to survive, according to resource dependency theory, organizations will alter their structure and change their goals, thereby changing their behavior (Pfeffer and Salancik, 1978). For example, in an analysis of unplanned change in nonprofit organizations, Powell and Friedkin (1987) conclude that external forces are likely to exert influence on organizational behavior when the organization faces a financial shortage, serves a constituency that lacks political clout, or is involved in activities that become increasingly complex. Although these cases relate to individual organizations, it is reasonable to assume that they reflect trends that affect particular segments of the nonprofit sector.

The implications of resource dependency theory underscore the ongoing debate over issues of autonomy and commercialization of nonprofits. In essence, there is a potential conflict between the established goals of the organization (i.e., the governing board, donors, and managers) and the goals of the newer revenue sources (i.e., government bureaus or fee-paying individuals).[5] Some fear that as governments rely on nonprofit organizations to help in the delivery of services through grants and contracts, the independence of the nonprofit sector is threatened. In competing for government grants and contracts, there is concern that nonprofits will become unduly influenced by the needs and requirements of government bureaus. In addition, as nonprofits increasingly generate revenues through charges for services, there is concern that they may neglect their original mission and ultimately lose their legitimacy.[6] To illustrate, we now turn to an examination of two industries in which different responses to changes in funding sources have resulted in different sectoral relationships and outcomes.

Financing and Sectoral Relationships: Two Cases

To explore how external financing decisions and organizational responses can affect sectoral relationships, we examine the hospital and higher education industries. These two cases are chosen because data are available for a considerable period of time and there has been an ongoing debate over the role of nonprofit hospitals and universities. We wish to emphasize that these cases are only illustrative and should not be construed as representative or exhaustive in their outcomes.

Hospitals[7]

Sectoral relationships and outcomes within the hospital industry have undergone major changes.[8] In the early part of this century, state, local and nonprofit hospitals played the predominant role in the delivery of health care. In 1928, state and local governments accounted for 12.5 percent of hospitals (general and short-term specialty) and 24.1 percent of hospital beds. By 1980, the percent of hospitals in the state and local sector had increased to 29.5, but the percent of beds had decreased to 20.5. The nonprofit sector accounted for 43.9 percent of the hospitals and 58.6 percent of hospital beds in 1929. The share of the nonprofit sector rose to 57.6 percent of hospitals and 70.3 percent of beds in 1980. The proprietary sector diminished over the same period from 43.6 percent of hospitals and 17.3 percent of beds to 13 percent and 9.2 percent, respectively (Hollingsworth and Hollingsworth, 1986: Table 1). Although much attention is currently focused on for-profit medicine, nonprofit hospitals still dominate the industry in terms of market share.

Differences in the relative market shares of the three sectors, however, conceal behavioral changes that have been occurring. Despite the increased nonprofit market share, the three sectors have increasingly similar input and output characteristics. In a recent study, Hollingsworth and Hollingsworth (1986) compare the three sectors in terms of operating and performance measures for three years-- 1935, 1961, 1979. Although distinctions among the three sectors continue to exist, they note the increasing similarity among different types of hospitals in terms of hospital size, percent of hospitals professionally accredited, length of stay, occupancy ratios, full time equivalent staff per bed, technological complexity, costs per beds, and assets per bed. Moreover, they are also more alike in the types of patients treated and the types of care delivered. Of these measures, distinctions among cost indicators, occupancy and length of stay have faded the most.

What are the reasons underlying the increasingly similar behavior of the three sectors? Hollingsworth and Hollingsworth acknowledge that the trend towards convergence reflects, in part, the increasing acceptance of medical technology, the standardization effects of accreditation, and the consensus about medical training methods. However, they believe that a greater source of similarities is the change in the funding sources of hospitals. In the early part of the period, public hospitals were funded primarily from state and local tax revenues, voluntary hospitals were funded primarily from charitable contributions, and for-profit hospitals were funded mostly from charges paid by patients. Different funding sources reflect different constituencies. Consequently, it is not surprising that in the early 1900's the behaviors of the three sectors were quite distinct. More recently, however, with the emergence of third-party reimbursement the funding sources of the three sectors have become more similar. Revenues have been increasingly derived from fees paid by insurance companies, Blue Cross, Medicare or Medicaid. As private and public insurance has enveloped the field, the distinctive behaviors of public, nonprofit and proprietary hospitals have blurred.

Universities

The higher education industry has experienced tremendous growth since the 1950's resulting in changes in the relative market share between the sectors. The growth was a response to increased demand for higher education fueled initially by the GI Bill and later by demographic forces. The demand was also affected by the emerging perception of a college degree as a vehicle for upward mobility. Although both the public and nonprofit sectors have grown, the expansion to accommodate the increased demand was carried out primarily in the public sector.[9] Consequently, the relative market share has changed. In 1950, the nonprofit sector accounted for 66 percent of universities and colleges and 51 percent of degrees. By 1982 the nonprofit share of the market had slipped to 54 percent of higher education institutions and 36 percent of degrees (American Council on Education, 1987: p. 110 and p. 152.) Nevertheless, the distinctive roles of public and nonprofit institutions have not eroded.

The fact that the public sector accommodated the majority of the increased demand reinforced the distinctive roles played by the public and nonprofit sectors. Public universities and colleges, with low tuition, provide education to large numbers of students, particularly students with limited income. Thus, they play a large role in ensuring that students with the appropriate academic credentials have access to higher education. In addition, public higher education provides an array of services to the public at large by generating professionals and knowledge aimed at stimulating state economic development. On the other hand, nonprofit institutions are viewed as providing high quality and diverse educational programs (Geiger, 1986).

The respective roles correspond to the funding sources of the two sectors. In terms of current fund revenues, nonprofit institutions receive the largest portion of their revenues from private sources. Tuition and fees accounted for 41.6 percent of revenues in 1950 and has decreased slightly to 37.5 percent in 1982. Governments provided only 11.2 percent of revenues in 1950, although this had increased to 19.5 by 1982, primarily due to increases at the federal level. In contrast, public institutions are highly dependent on government revenues. In 1950, they received 51.9 percent of their revenues from public funds (9.6 from federal sources; 37.4 from state sources). By 1982, public support increased to 60.3 percent (11.4 from federal sources; 45.3 from state sources). Tuition and fees accounted for only 18.5 percent in 1950 and decreased to 13.5 percent by 1982.[10] Thus, despite the expansion in the higher education industry, the revenue patterns of the two sectors have remained essentially the same. Not surprisingly, the two sectors still continue to make distinct contributions to higher education.[11]

Summary

Although causality is difficult to establish, the correlation in these two cases between financial sources and mission is evident. The sectoral differences in the market for higher education might well have been changed if the states had decided to accommodate the rising demand by providing financial incentives and support for expansion to nonprofit institutions rather than by expanding and creating public institutions. The evolution of the hospital industry provides a sharp contrast. The increased demand for hospital has been accommodated in all three sectors by third-party reimbursement rather than simply an expansion of the public hospital sector. Consequently all three sectors are able to compete for fee-paying patients. This has resulted in the diminution of differences between the nonprofit, public and proprietary hospitals.

This discussion of the relationship between financing and mission brings into question public policies which assume the distinctiveness of the nonprofit sector. It may be that for some industries the unique roles of the nonprofit sector within the industry may no longer exist. In that case, blanket support of the nonprofit sector may be unjustified. In order to assess whether such policies are warranted, we next consider the rationale for current policies and future prospects for these policies.

Implications for Public Policy: Today and Tomorrow

The most important public policies with respect to the nonprofit sector are their treatment under the tax code: federal, state and local. Simon (1987) has estimated that in 1985 nonprofits generated $100 billion in revenues which were exempt from federal income tax, held $300 billion in property exempt from state and local property taxes, and received $50 billion in contributions which were deductible for the donors from their federal and state income tax liabilities. Thus, tax advantages conferred upon the nonprofit sector represent a substantial monetary value to nonprofits. At the same time, they entail a considerable tax expenditure, i.e., a loss in tax revenues, by the public sector. The magnitude of these tax expenditures, in conjunction with an emerging perception of the nonprofit sector's loss of distinctiveness, raises two questions: 1) Should the nonprofit sector continue to receive tax preferences? and 2) If yes, what is the proper basis of such preferences? We address these questions by considering the rationale for current policies and speculating about future policies.

Rationales for the Current Tax Policies

Justification of the favorable treatment of nonprofit organizations and their donors has taken two different approaches: proper definition of the tax base and the desirability of stimulating nonprofit sector activity via subsidies.

The tax-base rationales vary in detail by the type of tax, e.g., individual income tax, corporate income tax or property tax, and the recipient of the tax advantage, e.g., nonprofit organization. Simon (1987) reviews the numerous arguments. For example, the deductibility of individuals' charitable contributions is defensible on the grounds that it is not a part of the Haig-Simons definition of taxable income.[12] Likewise, since contributions by corporations are not a form of profit, there is reason to provide deductions via the corporation income tax. The reasoning underlying the defense of the tax-exempt status of nonprofit organizations is somewhat different. Bittker and Radhart (1976) argue that nonprofits should not be taxed under corporation income tax statutes because the corporation tax is based on income-generating activities pursued for personal gain and, thus, is not relevant to nonprofit entities.

Although there is merit to the tax-base arguments, they do not appear to have been definitive in shaping public policy, particularly in the formative years. For example, the specific design of the tax system, e.g. limits of deductibility, does not appear consistent with this line of reasoning. The more prominent defense of the nonprofit sector's tax advantages is related to the notion of government support. The rationale for supporting the nonprofit sector is based on the notion that the services delivered by such organizations are collective in nature. In effect, the services yield benefits which are not restricted to the donors or the clients. Thus, in order to achieve a more efficient outcome, public action is required. There are two principal forms such action may take: 1) direct public delivery or 2) public support of private delivery. The former is preferable if the services are nonexcludable or the majority of the benefits derived from the service are nonrival. On the other hand, if the service has a mix of collective and private benefits and is excludable, the private sector, either for-profit or nonprofit, can organize the production and exchange of the service. The public sector, in turn, can bolster the activity via grants or tax subsidies. The historical record is replete with evidence for the support rationale. In fact, Simon quotes a recent Supreme Court opinion that asserts that tax exemption and deductibility are a form of subsidy having effects similar to government spending programs (461 U.S. at 544-5).

The tax subsidy approach allows public policy to build upon private behavior

Donors influence the value of the preferential tax treatment to nonprofits by the amount of contributions they make. In addition, clients who purchase services influence the value of the exemption afforded directly to the organization. Consequently, organizations who satisfy their constituents' preferences are rewarded. This results in diversity, one of the acclaimed attributes of the nonprofit sector. On the other hand, it relegates the public sector to a rather passive role. Moreover, rather than allocate resources for collective purposes via the government arena, it allows for such a determination by individual behavior, a behavior which is limited, in practice, to relatively high income individuals.[13] To the extent there is a collective interest in the activity, a sizable portion of the population is effectively precluded from participation. Thus, the basic issue is whether support for activities of the nonprofit sector should be assigned to the "domain of rights" or the "domain of dollars" (Okun, 1975).

Public Policies in the Future

Two propositions underpin current public policy toward the nonprofit sector: 1) the nonprofit sector performs functions which are socially desirable and, hence, deserving of public support; and 2) such support will primarily be in the form of tax subsidies. Unless such propositions are rebuffed, future policies are unlikely to depart radically from current policies, but neither are they likely to remain unchanged.

Our discussion of the fading distinctions among the three sectors hints at the possibility of undermining support for public subsidy of nonprofit organizations. Although the nonprofit sector has played a critical role in the development of American society, there is concern that the distinctiveness of the nonprofit sector, at least in some industries, is eroding. If the nonprofit sector begins to resemble public organizations, one may question whether it is desirable for public policy to create competition or underwrite duplication of public agencies without providing the means for public accountability. Likewise, if the nonprofit sector begins to resemble the proprietary sector, one may question whether it is useful for the public sector to underwrite activities which the for-profit sector is able and willing to organize and thus provide unfair competition.

It is unlikely, however these questions are answered, that the public policy of subsidizing the nonprofit sector via the tax system will be revoked. The differences among the sectors are not likely to be completely eradicated, but rather minimized. The public policy question then is at what cost should such distinctions be supported. Consequently, it is more likely that the various tax provisions will be subject to increased scrutiny. Such scrutiny may lead to a more discriminating application of tax subsidies.

If one accepts the assumption that the distinctiveness of the nonprofit sector is desirable, public officials are likely to look for policies designed to maintain that distinctiveness. The nonprofit status of an organization is not immutable.

For example, in the hospital industry an increasing number of nonprofit hospitals are converting to for-profit status. In addition, there are local governments which have chosen to spin off their hospitals to specifically created nonprofit foundations. Likewise, at various times nonprofit universities have been converted to public universities.[14] This suggests that the conferral of tax benefits needs to be based on performance rather than merely a legal definition. In effect, industry classification and the willingness of directors to accept the nondistribution and reasonable compensation constraints should be considered necessary but not sufficient conditions for tax subsidies. Failure to target tax preferences to organizations which make a distinctive contribution is likely to erode public support for these policies.

Dimensions of performance which could provide a basis for a more selective treatment of nonprofits are the extent to which they: deliver services to the poor; contribute diversity as reflected by direct public support, i.e., donations; serve as a direct substitute for public production, i.e., government contracts or grants; or some combination thereof.

The adoption of a performance-based determination of tax-exempt status would entail costs. It would impose reporting requirements that organizations may feel are intrusive and burdensome. In addition, it would require an administrative structure to monitor the organizations as well as to review, on a systematic basis, the validity of the preferential treatment. To the extent that this is done within the context of the current Internal Revenue Service, the additional costs would be minimal.[15] At the same time, additional benefits, in terms of added revenues, as well as more socially desirable outcomes, would accrue.

Conclusion

Although this analysis has been speculative, it does outline the issues which need to be addressed as public policies toward the voluntary nonprofit sector are reconsidered. They include both positive and normative questions. First, is the performance of nonprofit organizations distinguishable from public bureaus or firms? Second, if it is, to what extent is society willing to support the unique contributions of the nonprofit sector through public policies? Third, is it feasible to formulate and implement public policies which encourage the desirable contributions of the nonprofit sector rather than simply the nonprofit sector? The answers to these questions are likely to shape the debate about the future of public policies toward the nonprofit sector.

Notes

[1] Kramer (1981) has identified these as: pioneering, promotion of volunteerism, advocacy, and service provision.

[2] This category is distinct from mutual-benefit nonprofits which primarily create benefits for their members, and foundations which seek to achieve the delivery of collective services through their donations. For further elaboration of types of nonprofits see Simon (1987).

[3] This heterogeneity is reflected by the lack of a strong consensus about the motivations of nonprofit managers in contrast to the general consensus of the motivation of public managers, i.e., budget maximization, and for-profit managers, i.e.,profit maximization.

[4] While much attention is focused on the increased role of fees in the balance sheets of nonprofit organizations, there is also an increasing interest on the part of public institutions to expand their fundraising activities beyond legislative bodies. For example, California's public universities and colleges have long had an informal agreement with California's private higher education sector to limit their fundraising activities to alumni and traditional corporate friends. However, that agreement seems to be being ignored as the public institutions have decided to no longer merely rely on legislative appropriations (Los Angeles Times, 1987).

[5] This discussion is based on the long held stereotype of nonprofits as organizations formed by individuals to satisfy collective demands. More recently, a set of nonprofit organizations have formed to serve primarily as a conduit for government grants. This gives rise to the notion of third party government (Salamon,1987).

[6] It is also possible that the commercial endeavors will enable the original mission to be maintained by using the revenues collected from paying consumers to subsidize non-paying clients or nonprofitable activities. For a discussion of this model of nonprofit organizational behavior, see James (1983).

[7] This section is based largely on the work of Hollingsworth and Hollingsworth (1986).

[8] For a discussion of the changing nature of the three sectors in the emergence of the general health care field, see Marmor, Schlesinger and Smithey (1987).

[9] In the United States, universities and colleges are found only in the public and nonprofit sectors. There are virtually no for-profit institutions except for vocational education.

[10] Source: Nelson, 1978: pp. 70-1 and American Council on Education, 1987: pp. 46-49.

[11] The distinctiveness within the higher education industry is not simply limited to sectoral differences. Nonprofit universities and colleges serve a variety of functions which are largely attributable to different revenue sources. Geiger (1986) has identified three segments of the nonprofit sector, with different missions and revenues patterns: research universities, liberal arts colleges, and urban universities.

[12] According to the Haig-Simons definition, taxable income is defined as the sum of the individual's consumption and the accumulation of wealth. The individual's net worth is not increased as a result of the contribution. Thus, the question is whether the contribution represents a form of consumption. Since the individual does not benefit directly from the contribution, most do not consider it consumption. On the other hand, if one adopts the Weisbrod (1977) notion of nonprofit organizations as a response to unsatisfied collective demands, one is likely to arrive at the opposite conclusion.

[13] Lower income individuals are less likely to contribute due to their limited household budgets in general, and the relatively higher price of giving due to the use of deductions rather than credits for making adjustments to tax liability.

[14] Although there are a variety of reasons for such changes, financial considerations appear to be overriding. Organizations, by altering their legal form, enhance their access to financing sources. For-profit status opens up equity markets as a funding source. Government status enables the organization to compete for part of the public budget. On the other hand, conversion from government to nonprofit or for-profit form is a method for the public sector to reduce its financial commitments.

[15] It may be inappropriate for the Internal Revenue Service, whose primary goal is to collect revenues, to have the power to grant exempt status. On the other hand, a separate agency to grant exempt status is likely to substantially increase administrative costs.

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WORKING DRAFT

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THE SHIFTING BOUNDARIES OF THE INDEPENDENT SECTOR

by

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INTRODUCTION

What I have come to call "topographic maps" of the third sector (Van Til, 1988) are conventionally drawn on the basic of certain differences between major societal sectors. Corporate, governmental, voluntary, and household activities are seen as distinct in their purpose, activity, and implications. This view of sectoral distinctiveness presupposes the presence of boundaries between the sectors, as the cartographic position, in particular, suggests. The presence of boundaries gives rise to both imprecision and conflict along its lines. The purpose of this paper is to pose the issue of sectoral boundary definition, and to explore relations between major institutions.

The analysis of boundary issues will be helped by the setting of a framework, and the work of Talcott Parsons provides one admirably. Parsons (1966) identified four institutional sectors as central organizing structures of modern society. These institutions were seen to perform the four major tasks of societal development and maintenance, which Parsons identified as adaptation, goal-attainment, integration, and latent pattern-maintenance.

Parsons explained that the problem of adaptation, of securing the economic resources needed to establish the basis of societal existence, is assigned to the economy. The problem of goal-attainment, of achieving the ends deemed crucial for societal development, is the task of the polity. The third task, integration, involves linking disparate social groups and is the focus of the integrative sector. The final task, latent pattern-maintenance, is that of achieving meaning and coherence, and is the work of the cultural institutions of church, school, and family.

Parsons' four sectors translate roughly into the three sectors conventionally identified, with the "third sector" arrayed across his third and fourth (and sharing that latter region with the household). Such associations as churches and cultural organizations fall into this fourth sector, as well as such clearly non-third-sector organizations as households and schools (what British social scientists have come to call the "informal sector").

The Parsonian model suggests that the third sector is inhabited by organizations whose central focus is either influence or commitment, and perhaps by some organizations whose focus involves a blending of the two forces. Thus, pressure groups and lobbying organizations are quintessentially involved in influence. And, on the other hand, churches and arts leagues are predominantly guardians of commitments to larger systems of meaning. Perhaps it is in the blending of the two principles, when the church group takes a stand for social justice, or the arts league seeks to involve itself in the extension of arts education in the public schools, that the full potential of the third sector is realized.

To be sure, there remain many influence associations that are members of the first or second sectors, essentially appendages of business or governmental life (perhaps trade associations and political parties are the best examples). And just as certainly, many commitment-based associations should not be considered as part of the third sector, such as households and schools. The boundaries between the sectors may not take the form of precise lines, but rather may involve wide swaths of indeterminate territory, and considerable conceptual, as well as organizational blurring. The role of organizations on the margins of the state has been studied by Sharkansky (1979:145) who finds that "much proliferation of administrative bodies" on these margins. This organizational "blurring" solves some problems, he concludes, but creates others—most notably increasing the "incoherence" of government and policy.

Parsons approaches the question of sectoral boundaries by examining transactions between the major sectors. His model of the social system provides a powerful way of perceiving the boundaries between institutional sectors in society. Using his approach as a point of departure, but not necessarily as a theoretical strait-jacket, let us now proceed to examine the state of boundary relations between the voluntary sector and other institutions in contemporary society.

BOUNDARIES IN FLUX

Among the boundaries that may be seen in flux are those between the third sector and, respectively, government, business, and the household. This paper will pass lightly over these junctions, and then focus on the intersection of all four sectors, a point at the very nexus of our complex modern society.

Government and The Third Sector

As for the shifting boundary between government and the third sector, it is important to consider the rise of "third-party government" with its treatment of nonprofit organizations as contracted service providers (Sharkansky, 1979; Salamon, 1987; Billis and Harris, 1986) and the widespread presence of voluntary action within government (Cf. DeLaat, 1987; Sundeen, 1987).

Relations between voluntary associations and government may be viewed as being of two major types—formal and policy-related. Key among the formal relations are questions of charter and tax exemption. Governmental agencies review the applications of third sector organizations to determine their eligibility, under the tax code, and then proceed to review this eligibility on an ongoing basis. The income tax law determines which forms of charitable contributions may be properly deducted by individual givers from their tax liability. Foundations themselves are regulated by law as to their practices and reporting. Additionally, certain voluntary associations are deemed appropriate, and others inappropriate, to be favored by governmental support through grants, contracts, or the use of publicly-owned spaces and buildings for their meetings and activities, while others are denied access to these privileges.

When a government is controlled by individuals possessed of a particular ideological bent, the voluntary sector may be the subject of considerable interest and scrutiny on the part of governmental leaders. Such policy-related activity has characterized the Reagan administration, which has sought in a determined fashion to keep a number of politically-active organizations off the list of eligible donees for government-based charitable drives. The notorious OMB Circular 122 was one of several "federal policy iniatives...designed to curb specific types of politically active voluntary associations" (Wolch, 1986: 479).

The Reagan thrust to defund voluntary associations not deemed to act in accordance with its own conservative ideology has been joined to its frontal assault on the welfare state. The effort to severely restrict the reach of public welfare has led to the dual policy of governmental cut-back and the restriction of funding of non-profit service providers. This history, amply recounted and documented by Lester Salamon and associates, finds positive form only in the theory of "privatization" (Cf. Savas, 1981). This theory, essentially one of private sector supremacy over both government and voluntary organization, has fueled one of the more interesting boundary conflicts of the 1980s, that between small business and nonprofit corporations.

The Third Sector and Business

If it is true, as Ronald Reagan's favorite predecessor in the White House contended, that "the business of America is business", then the effort of the Small Business Administration to discredit nonprofit activity will not appear surprising. Corresponding to Coolidge's dictum is the unspoken assumption that the business of government is to serve largely as a watchman, assuring domestic stability and international hegemony. And the result for third sector organizations, as Ralph Kramer's (1981:273) "reprivatization" model implies, is to join the domestic functions of government in severe decline.

The boundary between business and nonprofit activity is often crossed, and DeLaat (1987) identifies four major ways in which work and volunteering are commonly connected:

> 1) volunteering is supplemental to primary work roles, and often compensates for needs not met in the work role situation; 2) volunteering is *instrumental* to primary work roles, or helps in the achievement of career objectives; 3) volunteering is a form of *expanding* the work role by doing additional, unpaid labor somehow related to the work role; or, 4) volunteering is, in itself, a conscious work activity.

Whatever the fate of the legislative initiatives taken by small business spokespersons to restrain nonprofit enterprise, there seems little question that in the 1980s an increasing number of nonprofit organizations increasingly have come to resemble "tax-exempt businesses". How much of their "teleological priority" (to use Gamwell's <1984> term) has been compromised in this process, and how far it will lead to a bifurcation of the third sector (Cf. Henry Hansmann's paper elsewhere in this collection), is yet to be seen, but once again the drift of change seems to be away from a clear set of sectoral distinctions.

The Voluntary Sector and the Household

Perhaps the blurriest of all the boundaries between major sectors involves that between the voluntary sector and the realm of informal social activity, such as the household and the neighborhood. Parsons' scheme, it will be recalled, places the voluntary sector squarely in the middle of the integrative and commitment sectors of society—including both influence groups and churches. The household itself, and the institutions that directly surround it and direct themselves to the task of sustaining families and nurturing individuals as they develop — the school, the church, and the community — are typically perceived as distinct from the voluntary sector, although voluntarism is seen to spring from these structures in the form of parent groups, church-related organizations, and neighborhood associations, respectively. The central point though, is that the solidary organizations that are most basic to any society — the family, the church, and the community — are linked to the larger society by the voluntary associations they generate as well as by the economic organizations that provide their members employment. Hence their common identification as "mediating structures", institutions that link individuals in their solidary structures of family and community to the larger world.

The voluntary associations that bloom from the rich soil of family need and aspiration, religious conviction, and neighborly interaction are overwhelmingly informal and even intermittent. Donald and Rachelle Warren (1985) have documented the significance and extent of "problem anchored helping networks" in U.S. society. Their research shows how individuals seek help when problems arise in ever-widening circles that begin with the immediate family, and then move toward friends, neighbors, co-workers. Less than ten percent of these problems are brought to the attention of governmental or private professional service-providers, or to clergy or co-members of a voluntary association.

Some of the problems that are dealt with through such networks are ongoing, such as the provision of child-care by the sharing of parent time and home space, or the meeting of shopping needs of a home-based invalid by one or more friends and neighbors. On some occasions, though not all, these networks will be signified by a group name. Only rarely will the group move toward formal incorporation, and join the ranks of certified nonprofit organizations within it its state.
The ability of voluntary organizations to form and reform, to hold constant and change, to stay informal and to move toward formalization, assures that the voluntary sector will remain a many-faceted and diverse one. In its flexibility of form and purpose lies an ability to meet many needs, both old and new and both large and small. It is in the ability to shape the cloth to genuine human needs that voluntarism particularly distinguishes itself.

At the Four Corners

An intersection not discussed by Parsons is formed at the common junction of the four sectors, a point of convergence at which philanthropic institutions stand particularly. At this boundary money is simultaneously traded for power, influence, and the commitment of values. Saved from the earnings of "private" economic activity of individuals in first-sector institutions, philanthropic contributions are removed from household expenditures to serve the advancement of the common good. Sometimes aimed at the funding of influence, or advocacy, organizations, and sometimes directed to the funding of social service or income transfer itself. The greatest portion of U.S. philanthropy sustains value-based organizations, particularly churches.

The boundary area between the four sectors that is philanthropy gives rise to a wide range of problems and interpretations. For some, the crucial issue is the persistence of altruism in an age of narcissism. What seems notable from this perspective is the continuing willingness of some individuals, families, and firms to maintain their participation in a tradition of giving (Cf. Karl, 1986; Odendahl, Boris, et al, 1987); Galaskiewicz, 1985). To others, the critical issue is the use of philanthropy to sustain privilege, its focus on the funding of a societal and value base designed to sustain structures of capitalist inequality (Cf. Alchon, 1986; Berman, 1983; and Schervish, Herman, and Rhenisch, 1986).

Schervish, Herman, and Rhenisch note that the problem of philanthropic influence is not a trivial one: "Through concerted philanthropic efforts, the wealthy, for good or for ill, for progressive or conservative ends, actually produce (rather than simply run or influence) the organizational world at the cutting edge of society" (1986: 226). Philanthropy involves, they assert, an "intricate interplay between structure, culture, and practice" (1986: 227).

The contemporary phenomena of "celebrity voluntarism" and "cause-related marketing" provide telling instances of the kind of intricate interplay that emerges between the four major sectors in modern society. Such philanthropic events as the "We Are the World" phonograph record, the "Live-Aid" and "Farm Aid" concerts, the worldwide "Run for Africa", the "Hands Across America" connection, and the restoration of the Statue of Liberty, and the provision of "Comic Relief" all took place in the mid-1980s with film and music performers playing leading roles and the media providing organizing services and heavy coverage. Meanwhile, numerous corporations have sought to advance their sales by committing a small proportion of gross receipts to one or another visible and "acceptable" charitable cause, thereby introducing a note of philanthropy into the prosaic world of household consumerism.

Ostensibly, such activities should be considered instances of voluntary action. They involve the financial and time contributions of many thousands, or even millions, of participants. They receive support in terms of released time and money from economic enterprises. Leading politicians, even including the President, join in supporting and participating in the activities. And the events involved in celebrity voluntarism are organized by hastily-constructed nonprofit organizations led by charismatic broker-administrators, often on leave from well-paying positions as entertainment brokers.

The four sectors clearly join hands in such activities. Business, government, voluntary organizations, and the household are linked by the common nexus of the mass media and the arts they purvey, particularly rock music and film.

Such activities are controversial forms of voluntary action, subject to satire and question. Humorist Garrison Keillor makes of his "Jack Schmidt, Arts Administrator" a character not unlike the "private eye" of the pulp novels of an earlier era. Newsweek asks: "Can millions of Americans really help the nation's hungry and homeless by joining hands for 15 minutes? Was it Woodstock Without Guilt—or the stirring of something deeper?" (June 2, 1986: 18). And in Britain, a principal organizer of the 1970's "Rock Against Racism" (Widgery, 30 May 1986) offers the following critique of the work of Live-Aid's organizer, Bob Geldof:

> Under the punk trappings, Band Aid faces the oldest of the fundraiser's problems. It is bound to think in terms of aid rather than political change. And that very thought process, central to the charitable approach, undermines the recipients to the exact degree it ennobles the donors. We could feed the world, plant the Sahara with peaches and potatoes, control the weather, harness the elements and protect against the locusts and the droughts. But this involves taking power out of the hands of the tiny elite who govern the world, east and west, rather than giving to those who, at present, endure the consequences of their irresponsible rule.

The gains of celebrity voluntarism and cause-related marketing are found in the awareness it creates of the magnitude of social problems, the opportunities (however fleeting) it provides for the manifestation of concerns and the joining with others of similar inclination in an expression of those concerns, and in the (highly variable) proceeds generated that actually reach and improve the lot of those suffering under the problem at hand.

Moreover, if one believes in "going with the flow" of social change, then why not "privatize" philanthropy as well as everything else in society? If the business of America is business, why not hawk philanthropy along with everything else? As a recent "society figure" who became a "celebrity" for running a house of prostitution put it when asked if the public revelation of her past had ruined her life: "Do you know how much better my life is? The number and quality of opportunities open to me now so far exceed those that would have been available to me had I gone down another road. I'm sure it upsets people when they hear me say that....they think, 'here is someone who did something bad and she is making out like a bandit.' But hey, that's America"<1> Stay tuned—perhaps she will soon announce the formation of her own foundation. Hey, that's America!

The costs of celebrity volunteerism may be identified, as sociologist Robert Hunter has perceptively noted (personal conversation, 1986), in an interruption of the "social problems cycle". Rather than a problem moving from stages of awareness and initial response to organization and resolution, action may become immobilized in the false belief that a single event or miniscule credit-card "donation" has sufficed to resolve a problem. "Compassion fatigue" or the sense of being "aided out" may emerge, further slowing the course of social change. And corporate giving may be increasingly channeled only to causes that provide widespread advertising of the benevolence of the donor, thus reducing corporate interest in providing less visible philanthropy than that which provides it access to such venerated, and widely-viewed, symbols as the Statue of Liberty Thus, leaders of African relief organizations have begun to point to a widening gap between need and charitable resources as the problem of African famine fell from the narrow peak of public and media concern.

Celebrity voluntarism, with its aura of faddishness and its close ties to the entertainment industry, may itself fall quickly from the peak of attention it has received. Straws in the wind may be discerned in the fund-raising innovation of the "non-ball". After all, even the wealthy enjoy not dressing up and spending an evening at home with the VCR, at least now and then.

In a scholarly study to the point, Susan Ostrander explores the interaction between class and gender as the upper-class women she studied approached voluntary action. One of her respondents, Mrs. Holt, "expressed the generally shared view that private money is somehow less constrained than public money: 'Private contributions are necessary in a democracy. It has a freer hand than public money.' At the heart of volunteerism and the role of private money in protecting the 'American way' is the issue of private control, or private power" (Ostrander, 1984: 132-133). Ostrander continues: "These women are highly conscious of class. They have a genuine class analysis that they use to make sense out of their own lives, and they speak highly of the joys of their material standard of living and the freedom it gives them. They enjoy the pleasures of coming from well-known and well-respected families. And they appreciate the advantages of having direct and informal access to persons in positions of power who are their class, if not gender, equals" (Ostrander, 1984: 152). Volunteerism and philanthropy do indeed stand as part of an intricate interplay between structure, culture, and practice.

The meaning of philanthropy—altruistic concern or manipulative protection of privilege and position—continues to rage as a debate among voluntary action scholars. Like other issues that involve the major perspectives at contest among social scientists, this one will not be resolved by simply waiting for "the facts". It is actively linked to the ways in which we define voluntarism, and to the boundaries we draw about it.

CONCLUSION: THE IMPACT OF SOCIAL TECTONICS AND CLIMATE ON THE BLURRING OF BOUNDARIES

The argument of this paper has shown the boundaries to be blurred and the activities of sectoral organizations interdependent. How can the argument be sustained that this blurriness and interdependence is in any way related to forces of deep structure or values in society?

The way to make the argument is by noting the static nature of the conventional three- (or four-) sector conception. If the organizational world is divided into three (or four) sectors, we are given no indication as to why each sector takes the form and magnitude that it does. Nor are we given any cue as to why one or another sector might expand, contract, or be subject to organizational stress. And evidence of blurriness between the sectors similarly stands incapable of explanation by the conventional approach.

Once what I call "tectonic forces" are introduced into the model, an important dynamic is provided. Now it becomes possible to relate the structure of the voluntary sector to prevailing and emerging forces at work in the political and social economies of differing societies. The relative expansion or contraction of levels of national wealth, of tax policies, of spending priorities, and of governmental capacity may now be assessed and added to our understanding of the shifting boundaries between the major sectors. The blurring of boundaries becomes understood as a function, at least in part, of shifting forces in the basic political and economic substructures of society.

Moreover, when what I call the "climatic" forces, those that comprehend the prevailing and emerging values of society are added to our consideration, important understandings present themselves regarding the workings of the voluntary principle in society. Now we begin to understand how the predisposition toward societal concern can infuse not only voluntary organizations, but governmental and economic institutions as well. The blurring of boundaries is thereby explained in yet a greater part by understanding the ways in which differing conceptions of valued action wax and wane with the shifting societal climate.

If a genuine role for voluntarism is to be found in society, topographic conceptions will have to join with basic tectonic and climatic realities. Thus a clear eye will be required to assure that the three sectors are not hypostastized, but are recognized as being overlapping and even occasionally blurred constructs on the landscape of human endavor. And a simultaneous concern will be required to assure that the deeper forces of economic development, decay, and control, political guidance and decisions, and cultural signification and shift are attended as well.

Recognizing that the institutional topography of modern societies does not permit the easy distinction between what is corporate, government, third sector, and household is a beginning. The third sector, we have seen, is closely linked to each of the other sectors. At times it takes a form not dissimilar from a business; at other times it exercises the functions of government; and on the neighborhood level, it blends with the household in the meeting of local and family needs.

This blurring of the sectors gives voluntarism an opening to permeate the other sectors, introducing them to the transforming powers of democratic control, concern with values, and the courage to create change. When the corporate executive calls upon the skilled volunteer to help develop structures for employee participation and control at the workplace, the powers of pervasive voluntarism will be seen. When the political leader calls upon the neighborhood associations to develop an agenda for legislative change that will then be supported, then the powers of pervasive voluntarism will be exercised. When the working mother calls upon the United Way to recognize that the future of her children depends upon the quality of after-school and emergency illness care, then the powers of pervasive voluntarism will become real. It is for reasons such as these that the boundaries of the third sector, imprecise and blurry as they often are, deserve the close attention of scholars and practitioners alike.

NOTE

1. Jill Gerston, "Success from Scandal." The Philadelphia Inquirer, September 22, 1986, E-1.

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THE NONPROFIT AS THE FIRST SECTOR: POLICY IMPLICATIONS

by

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The Nonprofit as the First Sector

Background

It is now well appreciated by scholars and others concerned with contemporary nonprofit organizations that the nonprofit sector struggles with an identity crisis. Indeed, Jon Van Til (1988) has just written a whole book devoted to coping with this question from a theoretical standpoint. We designate the sector by what it is not, but have difficulty finding a term that describes the sector in a positive way. "Voluntary sector", "independent sector", and "mediating institutions", for example, are the most popular terms that have fallen to the realities and complexities of modern day nonprofit organizations, as significant numbers of these organizations rely on paid staff, are highly reliant on the public and business sectors, and serve not merely as intermediaries but as primary service providers.

The "third sector" is another term that has been employed, if not with great enthusiasm, by those who seek an accurate and if bland and neutral description. Yet even this term has its problems for there are several dimensions along which the sectors may be ordered, and it is not clear that the nonprofit sector comes out third on each one. Certainly if measured in terms of the volume of economic activity, e.g. by income, expenditures, assets, or employment (but not volunteering), the nonprofit sector is third to business and government. But other ways of keeping score are equally valid. For example, a number of scholars suggest that, historically speaking, nonprofit organizations tend to precede the development of profitseeking or governmental institutions. Bremner (1960), Weisbrod (1977), and Mason (1984), for example, suggest that nonprofit activity foreshadows governmental initiative, while Mason (1984), Greene (1977) and others observe that nonprofits break the economic ground for business. In the historical developmental sense then, the nonprofit may be the first sector.

Alternatively, one can view the sectors from a normative point of view, as suggested by Gamwell (1984). As Van Til (1988) observes: "Gamwell notes 'a certain injustice' in ordering this special group of associations as the 'third sector'". Gamwell's point is that in terms of their high societal purpose, nonprofit institutions are morally superior, or in his term "teleologically prior" and deserve to be called the "first sector".

Perhaps the most troublesome dimension on which the nonprofit sector tends to rank third is its treatment in positive social science theory, especially economic theory. The best known economic theories of the sector, those developed by Weisbrod (1977) and Hansmann (1980), essentially view the nonprofit sector as a residual one, resulting from failures of government on the one hand, and the private marketplace, on the other hand. In these frameworks, nonprofit organizations arise to provide services with which the first and second sectors have difficulty. Recently, however, Salamon (1987) has put the shoe on the other foot, specifying a theoretical framework that he calls "voluntary failure". In this view, governmental activity is seen to arise out of the inadequacies of voluntary provision. Presumably, a similar construction could be developed to explain the rise of business enterprise.

In this paper, I will discuss the implications of viewing the nonprofit as the first sector in a sense that mirrors Salamon's ideas and which parallels the historical view. Namely, I will argue that the nonprofit sector is the more basic, primary sector, constituting the original medium in which organizations in any given field first develop. In this sense, it is a sort of undifferentiated "primordial organizational soup" which, over time, gives rise to certain specialized forms, e.g. businesses or governmental entities, that eventually occupy their own sectors. I will argue that this "evolutionary" perspective calls into question the present public policy treatment of nonprofit organizations. In short, this view suggests that the nonprofit sector, and its derivative sectors of business and government as well, contain within themselves a variety of potential motivations and behaviors. This raises the question of whether the label "nonprofit" is the best way of singling out organizations for preferential policy treatment tied to the provision of public benefits. The particular focus of the discussion will be on "mixed industries" in which similar services can be provided by businesses or government agencies as well as nonprofits.

Terminology

Before elaborating on the foregoing view, it is useful to distinguish among several concepts to be used below: industries, activities, purposes, motivations, constraints, incentives and behaviors:

An "industry" is a collection of organizations that provide the same general mix of services. Some industries cross sectoral boundaries, and many of these, such as the hospital or day care industries, involve the nonprofit sector. While some industries may involve nonprofit organizations exclusively, e.g. professional associations or religious institutions, in this paper we will be concerned mainly with industries, such as hospitals, day care centers, or theatres, in which nonprofits, businesses, and possibly government agencies, co-exist in the production of services.

"Activities" are services provided by industries. Organizations in many industries engage in several (usually inter-related) activities. For example, hospitals sponsor research, teach medical students, and provide treatment for the sick. Universities educate and do research, etc.

"Purposes" are the normative objectives associated with particular varieties of activity and with sectors within industries. For example, certain of hospitals' activities, such as research and charitable care for the poor, are oriented towards the general public good, while other activities, such as elective surgery emphasize the generation of private benefits. In present public policy treatment, nonprofits are expected to emphasize those activities with more public-regarding purposes.

"Motivations" are the personal reasons that energize and drive individuals to participate in organizations and take part in their activities. Motivations can range from greed to artistic achievement to altruism or belief in a good cause (see Young, 1983).

"Constraints" are the structural factors associated with given industries, and sectors within industries, that restrain the pursuit of particular motivations. For example, in the nonprofit sector, the nondistibution constraint is intended to restrain self-enrichment by those in control of the organization. "Incentives" are the reverse of constraints; they are structural parameters designed to encourage rather than discourage pursuit of certain motivations.

"Behavior" is the actual pattern of service provision in terms of quality, cost, reliability, and distribution of benefits among alternative recipient groups. Behavior results from the interaction of motivations and constraints or incentives, and is reflected in the nature of activities and purposes pursued by organizations in an industry.

Given these distinctions, we can now observe that one characteristic of many of the social science theories that seek to explain the existence of nonprofit organizations is that they tend to slide over the differences between the (normative) purposes of an organization, the motivations of its participants and the resultant organizational behavior. This gives rise to a largely schizophrenic literature on nonprofits: those who analyze the behavior of nonprofits usually base their models on selfish, utilitarian motivations of participants while those who try to explain existence of the sector cite normative purposes and assume a sectoral advantage in promoting virtue. Thus, while James (1983), Niskanen (1971), Pauly and Redisch (1973), Rose-Ackerman (1987) and others explain nonprofit behavior in terms of maximizing income, power and status, or other utilitarian benefits to managers, Hansmann (1980) reasons that nonprofits exist because they are more trustworthy than profitmaking businesses and Weisbrod (1977) argues that nonprofits accommodate the collective good of groups within communities that do not command a political majority. Salamon too sees nonprofits as public-regarding, but in partnership with government, while Berger and Neuhaus (1977) view nonprofits as public-spirited units that connect the powerless individual to the mega-institutions of the public and business sectors. Clearly, it is on the basis of these latter presumed virtues, related to purpose, that nonprofit organizations are granted special public policy treatment.

How can the two streams of economic literature - behavioral versus theory of existence - be reconciled? The important concept for doing so is the distinction between the purpose of an organization and the motivations that energize it. The rationales for nonprofits developed by Hansmann, Weisbrod and Salamon, mainly concern purpose and the advantage of the nonprofit form for pursuing certain purposes. But these theories do not speak directly to motivation or behavior. Contributions to the literature on nonprofit organization behavior, on the other hand, generally assume some singular variety of motivation, usually selfish, and put the burden of behavior control on the constraints built into the nonprofit form.

In the view propounded here, it is assumed that the incentives and constraints applying to nonprofit (and other types of) organizations are not fully determining of behavior and that motivations do influence behavior. Moreover, I argue here that it is insufficient to assume that only a single variety of motivation, either selfish or altruistic, exists within a given sector and that each sector will accommodate a distribution of participant motivations and behaviors, rather than a singular variety. This argument follows from previous work (Young, 1983) in which I observed that entrepreneurs within a given industry are driven by a variety of motives that ultimately may manifest themselves in organization behaviors. Those motivations tend to sort themselves out by sector by a process of matching motives to the norms and opportunities of each sector. However, because this sorting process is imperfect, and is based on multi-dimensional sector characteristics, it yields not only modal differences in motivation between sectors but also substantial intra-sector variations. Thus, while the motivational content of sectors may differ "on average", (the tails of) sectoral motivation distributions may also overlap substantially. Hence, it becomes important to examine the range of motivations, as well as the modal type of motivation that may be attracted to organizations in each sector, if we are to obtain a full picture of sector behavior as well as inter-sector differences.

An Evolutionary Model

Here, I want to argue, in developing the notion of the nonprofit sector as the primary sector (primordial soup) from which alternative types of organizations develop, that the nonprofit is the most robust sector in terms of the motivations and behaviors that it may encompass, and that the business and government sectors, while more specialized, are also motivationally and behaviorally heterogeneous. It is this intra-sectoral heterogeneity that ultimately gives rise to the proposition that renewed scrutiny of differential public policy treatment of the sectors may be desireable. In order to develop this argument, I will consider a nominal scenario through which an industry evolves and differentiates itself into public, business and nonprofit sectors.

Basically, there are two stages in the

chronological development of an industry. In the first stage, an activity is pursued and organized in nonprofit form. At this stage, the activity is experimental and it is unclear whether it can be made profitable or whether a large enough coalition would support its provision by government. It remains in the nonprofit sector until these questions become clarified (Mason,1984). One reason for this is the nonprofit sector's intrinsic flexibility. Nonprofits can avail themselves of a wide spectrum of means of support and a wide variety of constituencies (Mason, 1984); hence, they constitute a flexible vehicle for accommodating diverse purposes. This is part of the reason why the nonprofit is "first" in the evolutionary sense described here. Once activities move to the business or government sectors they experience environments that are somewhat less flexible and tolerant of alternative purposes and concommitant behaviors.

While in this first stage, participants with a wide variety of motivations are drawn to the activity, some for its innovative character per se, some for its potential to promote social good, and some for the potential self-enrichment it may ultimately promise. As the activity progresses in this stage, the motivational mix is liable to become more heterogeneous. In particular, as the public good and profit potentials become clearer more individuals with motives consistent with these interests will be drawn in, even before those potentialities can be realized. The nonprofit form only loosely constrains those who would enter. All that is required is that participant organizations find some viable group of constituents to support them, whether by grants, donations, volunteeer labor, member fees, or the like. Thus, a wide variety of motivations may be accommodated within the nonprofit sector at this stage. And to the extent that it is viable, a range of private purposes and self-enriching behaviors as well as public-serving behaviors may be manifested within the sector because there is no stringent market or political test for survival.

In stage two, the profit potential or political viability for the activity becomes clarified, making it possible for some organizations engaging in the activity to operate within a business framework or within government. Some proportion of existing activity providers then move to these sectors, as the historical perspective suggests. (New providers may also enter.) In the process of this shifting, some of the motivations contained within the nonprofit sector are siphoned into business or government. There are several reasons for this. Although self-enrichment is feasible within the nonprofit framework, it may be more efficiently pursued in the business sector where explicit mechanisms of ownership and development of capital are in place. Moreover, there is a signalling phenemonon that occurs. In business, self-enrichment is condoned and encouraged. Individuals move so that their motivations match the prescribed norms. Similarly for the shifts of activity into government. While the public purpose is served by nonprofit organizations, it may be more efficiently pursued on a larger scale by government because of the nonprofit sector's free rider problem. (See Olson, 1965). In addition, while personal power objectives may also be pursued in nonprofit organizations, the potential for this goal may be richer in the public sector (Young, 1983). As a result, in stage two, the mix of motivations in the nonprofit sector becomes differentiated from that in business or government, within a given industry.

However, there are a number of reasons why this sorting process does not result in a clean separation of motivations by sector, or why the nonprofit sector does not always wither away in the evolutionary process herein described. In particular, the business sector may absorb some altruistic or public-spirited motivations as well as self-enriching ones, while the nonprofit sector may retain some selfish motivations.

Consider the mixture of motivations siphoning off to the business sector. In the first place, individuals themselves may internalize a mixture of motives. Since individuals move as whole beings, they will inevitably bring a mix of motives to whatever sector they work in. Second, activities with alternative purposes often cluster together so that when transitions of activity occur, they are accompanied by mixed motives associated with mixed purposes. For example, even in the business sector, hospitals will support research and teaching and these activities in turn will maintain participation of some with unselfish motives.

Similar arguments apply to the segment of activities "left behind" in the nonprofit sector. While certain levels of self-seeking motivation will be siphoned away from the nonprofit sector, that sector will not be fully "purified". Again, individual people internalize mixed motives. In addition, there is a certain stickiness or inertia to the process of transition. Unless the benefits are very clearcut and the entry barriers to business quite low, some self-seeking motivations can be expected to remain with the nonprofit context. Third, there is the possibility of willful exploitation of the nonprofit context; i.e., although normative signals and explicit structural mechanisms encourage self-seeking behavior to operate in the business sector, some participants may see opportunities to exploit the weaker accountability structure of the nonprofit sector in order to seek their fortunes. Hence, they choose not to select themselves out of that sector.

In summary, I argue that as industries evolve from their primordial stage 1 form in the nonprofit sector to become differentiated into other sectors at stage 2, the motivations within the nonprofit sector remain mixed. Moreover, motivations in the derivative (business or government) sectors are also not singular. While there will be average or modal differences in the motivational mix between sectors, it would also appear to be the case that substantial overlaps in motivational distributions would occur because of the factors discussed above.

Finally, note that the foregoing argument does not assume a fixed distribution of motivations in an industry over time, nor that it is possible to identify, in advance, which emerging activities will be profitable. In stage 1, there will be considerable uncertainty about the future of an activity. Thus, the activity will attract pioneers and risk-takers of various motivational stripes. Only in stage 2 will profit potential and public benefits become clear. At this stage, new entrants may bring with them different motivations than the pioneers, and a result, may change the motivational mix of the industry over time. Nonetheless, the motivational mixes by sector will remain heterogeneous for the reasons articulated above.

Thus far, however, we have argued only in terms of motives, not behavior. If constraints within the sectors are so tight as to preclude the manifestation of alternative behaviors, the above argument would be moot. Because businesses must make a profit from sales to survive, and because government activity must conform roughly to the preferences of a political majority or a controlling coalition, one may question whether the foregoing heterogeneous mixes of motivations within sectors are viable in the long run or make any difference in terms of observed behavior. If one views the business or government sectors as highly competitive and admitting only of singular varieties of behavior for survival, then the argument for behavioral heterogeneity in the business or government sectors is nullified. However, it seems more realistic to argue that competition in these sectors is not generally binding. Rather, the model of managerial discretion within which managers of businesses (Williamson, 1964) or government agencies (Niskanen, 1970) have flexibility in their behavior, seems more appropriate many cases. For nonprofit organizations, the case for managerial discretion seems even stronger. For example, Rose-Ackerman (1987) argues that substantial differences may exist between the preferences of charity managers and donors, and that the limited choice among charities provides managers with discretion to follow their own preferences. This argument is re-enforced by the fact that no clear performance criteria exist, analogous to profit or political support, by which donors or trustees can hold nonprofit managers accountable. Moreover, the nonprofit sector has no strong motivational filter of its own. All that is intrinsically required for a nonprofit to survive is that it be able to find some group of people willing to support its aims, good or bad, selfish or altruistic, and that it satisfy (if it so chooses) some very broad and unevenly policed rules to acquire a charter and official, tax-exempt status (see Simon, 1987). While there are strong religious, service, community-based, artistic, professional and other traditions contained within subsectors of the nonprofit community, no strong overall mechanism limits the nonprofit sector to a particular (virtuous) variety of behavior.

Add to this the now well-appreciated facts that: (1) the three sectors are highly intertwined in their relationships and dependent on one another for resources and services (Salamon, 1987); and (2) that as circumstances change, or as "errors" in sector choice are corrected, there are movements of activities from the government and business sectors back into the nonprofit sector which entail the same kinds of inertial tendencies and intermixtures of purposes and motives as movements in the other direction (see Legoretta and Young, 1986); and you are certain to reach Jon Van Til's (1988) conclusion that the acts of nonprofit organizations are not "... necessarily clothed in a special robe of virtue. They are human endeavors, and like the rest of them, require questioning, evaluation, and, at times, even regulation."

In summary, an evolutionary theoretical perspective would characterize the nonprofit as the first sector in the sense of it being more basic and general than business or government. The latter institutions arise as specializations to accommodate certain wealth-seeking and political purposes and tolerate a narrower, but still diverse, set of behaviors than the nonprofit arena from which they derive. The nonprofit sector, on the other hand, is purified of selfish motives in some degree by the divestment of activity into other sectors, but nonetheless retains a heterogeneous motivational mix and tolerates a variety of behaviors. Since the special policy treatment of nonprofits is based on an assumption of public-spirited, benevolently motivated behavior by these organizations, the evolutionary view suggests that a fresh look be taken at this policy structure.

Policy

If the nonprofit is really the first sector in the evolutionary sense that we have described, and given the implications of this model that both the nonprofit and other sectors will necessarily embody both selfish and public-regarding motivations and behaviors, then one is led to the conclusion that the present system for policy treatment of nonprofit organizations may be misguided. That is, public policy should encourage and reward publicly beneficial behavior wherever it occurs, and should not reward selfish behavior in the guise of virtue.

The present policy system, which may be termed "regulation by structure", grants corporate tax exemptions, tax-deductibility of charitable contributions, postal benefits, property tax relief, exclusive rights to provide services or receive contracts under certain governmental programs, and other benefits and subsidies to organizations that assume the nonprofit form. (It also offers certain tax and other benefits that only profitmaking businesses can use; however, my focus here will remain with the treatment of nonprofits.) The conceptual basis for the present policy structure has two complementary parts. First, it is assumed that the nonprofit form itself limits for selfish behavior. In particular, as Hansmann (1980) argues, the nondistribution constraint prohibits those in control of a nonprofit organization from appropriating for themselves, the financial surpluses of the organization. It is argued here, however, that the nondistribution constrain actually inhibits rather than prohibits. In particular, unless that constraint is intensively policed, which it is not in most cases (see Simon, 1987), then it will be possible to circumvent the constraint through various channels including outright cheating (direct profit-taking), inflated salaries, self-dealing in the supply of input materials and supplies and contracted services, or the provision of services that directly benefit those in control. These possibilities are not worrisome if it can be comfortably assumed that the intents and motives of those who in engage in nonprofit activity are pure. However, our evolutionary, first sector theory suggests otherwise.

Compensation for the "leakiness" of a poorly policed nondistribution constraint, and justification for the present policy structure, is partially provided by another conceptual pillar of the present system - that of screening and signalling. According to this argument, each of the sectors signal certain values represented by its stated norms and supporting opportunity structures. For business, that norm involves wealth creation and self-seeking behavior; for the nonprofit sector, the norm promotes the public good and collective action. Signalling theory proposes that organizational participants will seek that context which most comfortably fits and accommodates their orientations and objectives. Hence, there will be a natural sorting of motivations and behaviors into the different sectors, with the business sector, for example, attracting the income maximizers. (See Young, 1983). An important adjunct consideration to the signalling model, developed by Hansmann (1980), is that the nonprofit form, because of both its normative structure, the consequent screening of motivations that this structure sets in motion, and the presence of the nondistribution constraint, serves as a signal to consumers and contributors. They, therefore, put their trust in nonprofits and direct their contributions and patronage to these organizations in circumstances where they cannot verify the quality and integrity of services directly for themselves.

While the signalling argument may be valid in general way, it also has its "leaks". In particular, the theory describes where the "modal participant" with a given variety of motivation will choose to operate; it does not argue that a given sector will capture all motivational elements of a given type. Indeed, the first sector, evolutionary theory that we have discused here, suggests that motivational orientation and consequent behaviors will not be cleanly separated by sector. On average, the behavioral orientations of the sectors will be different, but there will be substantial variation within sectors. As a consequence, the present policy structure will reward some nonprofits that behave inappropriately while it penalizes some business behavior that may be in the public interest. The extent of this dysfunctional pattern is an empirical question; it depends on the extent of the leaks in the nondistribution constraint and the screening process in practice.

What are the alternatives to the present policy? One approach is to keep the status quo. If the leaks are relatively small, then it may be better simply to live with the imperfections of the present system. Examples can be cited of serious abuses by nonprofit organizations (e.g. see Etzioni and Doty, 1976) and of public-spirited behavior by businesses (e.g. see McKie, 1974), but a determination of how important these phenomena are in quantitative terms is not available.

Another nonradical approach, ofcourse, would be to increase the resources devoted to policing the nonprofit sector so as to reduce the serious leaks. This may be desireable if it turns out that a relatively modest investment in investigative machinery ameliorates a significant proportion of present misbehavior. However, this alternative would fail to address the possibility that businesses are inhibited under the present system in pursuing certain publicly beneficial behaviors.

The evolutionary, first sector theory essentially argues for a different approach, one that would directly reward publically regarding behavior with tax and other benefits, and deny such benefits when such behavior was not forthcoming, regardless of sector - in other words, a "sector neutral" regulatory policy. But what would such a system look like, is it feasible, and how might it be implemented? Two different conceptual bases might be considered: output regulation and process regulation.

A system of output regulation would essentially grant special benefits to those organizations, regardless of sector, that provide designated public services of appropriate quality, cost and distribution among those in need. Under such a system, hospitals, day care centers, schools, arts and cultural organizations, and organizations in other industries deemed to encompass a special public purpose or to be subject to "contract failure" deriving from consumer disadvantage, would be eligible for policy benefits, regardless of their sector, if they can convince regulators of their special merit. The problem with this alternative, of course, is that it puts a heavy burden on the regulators, one which, in general, they cannot adequately assume. There are several well-known problems with such regulation. The regulatory system may require an enormous allocation of resources to gather necessary information, in collecting such information it may become intrusive, and it will be subject to corruption by the regulatees. More fundamentally, however, for the kinds of services in which nonprofits have typically been engaged, adequate regulation of output is made highly problematic by the difficulties of measurement. In particular, the subtle aspects of service quality in such areas as day care, health care, or education, are not subject to quantitative specification. As the work of Weisbrod and Schlesinger (1986) on nursing homes demonstrates, organizations bent on self-enrichment will toe the line where performance can be measured, but will elude accountability where it cannot.

If "regulation by structure" (the present approach) is unsatisfactory, and if regulation of output doesn't work, is there another alternative? "Regulation by process" is such a possibility. One reason that people (consumers, donors, grantors, government contractors, etc.) rely on nonprofit organizations and entrust them with the provision of sensitive services is that their decisionmaking processes and records tend to be more open and accessible. Nonprofit day care centers or nursing homes, for example, are more likely to involve parents or children of the elderly in advisory groups or on their boards and to maintain an open house policy with respect to visitation. Nonprofit universities and health care organizations more commonly participate in professional peer review processes, and so on. As Nelson and Krashinsky (1973) have argued, this is an essential reason why the nonprofit alternative may be preferable in many cases. And processes tend to be much easier to specify and to verify than outputs. But note, there is no exclusive link between open processes of decisionmaking and a particular corporate form. Many nonprofit organizations are closed and secretive in their deliberations while many businesses operate quite openly and encourage the participation of consumer-oriented parties. Is there any reason, therefore, that a for-profit day care center that opens its books to public scrutiny and opens its program for public inspection be denied the same policy benefits as the nonprofit center that does the same? And is there any good reason to grant those policy benefits to the nonprofit nursing home that denies such public access? In principle, there is not, assuming that viable processes can be specified that will provide effective oversight.

Pursuit of a policy of regulation by process rather than regulation by structure, would require considerable study, industry by industry. The structure and functioning of governing boards, the specification and roles of advisory committees, the use of peer review and accreditation systems, codes of ethical practice, the processing of complaints and grievances, and the standards for accounting and publication of financial records and program reports, would all have to be examined. We would have to ask what processes help ensure a good school, a good day care center, a good nursing home? We may also have to consider breaking down exclusive structures such as accreditation processes that demand nonprofit status as a prerequisite to participation or approval. I suspect that, in the end, we would find that it would be mainly the organizations that are now nonprofit that would be best accommodated by a process model of regulation for determining policy benefits. However, we must also be open to the likelihood that some businesses would also qualify, that some organizations presently nonprofit would not, and that an overall net improvement in the systems for delivering essential public services may result.

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FUTURE RELATIONSHIPS AMONG THE SECTORS

by

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Prepared for the 1988 Spring Research Forum
"Looking Forward to the Year 2000:
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Introduction. In discussing the future of relationships between the Independent Sector and the two other major centers of institutional power in the United States -- business and government -- there is an almost irresistable temptation to embroider on the obvious. And the obvious is that, in the normal course of affairs, the future of non-profit organizations and activities will depend largely on whether the American economy achieves solid and sustained real growth in productivity and profits and whether government, particularly at the federal level, revives the spirit of activism that in the past has led it to come to grips with the nation's major social and economic problems.

There is nothing novel about this forecast. In this century, at least, the Independent Sector has prospered largely through partnerships with business and government. Business has been critical as a donor, creator of endowed organizations and customer for non-profit services. Also the general state of the economy, as reflected in business conditions, directly or indirectly determines how much real income Americans have available as well as its distribution, and hence the willingness of individuals to make charitable contributions. The role of government is critical for many of the same reasons. Lester Solomon and others have documented how dependent most Independent Sector organizations are on government grants and contracts for service delivery and research. 1/ And, of course, the areas of the sector that Solomon did not study -- health care and traditional forms of education -- are the most dependent of all.

Finally, the linkage among government, business and the non-profit world comes full circle when one considers that a major function of government at all levels is maintaining economic prosperity. And the rate of economic growth often determines how much Americans are willing to invest in government services -- as the influence of economic worries on both the Carter and Reagan administrations most recently has shown.

In short, when government and business grow, the Independent Sector grows too. When they slow down, it falls on hard times. Given this perennial linkage, I would like to describe two possible future scenarios for the Independent Sector and raise the possibility of a third.

Everything is rosy. First, let's imagine a rosy future. If we can work the present kinks out of the our economy, the United States could well experience a period of healthy economic growth well into the next century -- at least until the demographic burden of dealing with the retirement of the baby boom generation falls on us, and possibly beyond if we make adequate provision for that pivotal development. If this rosy scenario unfolds, businesses will reinvigorate their programs of corporate philanthrophy and public service. Some of their contributions obviously will go to the traditional beneficiaries of corporate largess: educational, research, cultural and local improvement efforts in the communities where particular companies have their operations, or in areas of endeavor in which they perceive at least some indirect self-interest.

But one can also anticipate new twists in business support. Many large companies are now coming to realize that it is very much in their self-interest to help their employees deal with a wide range of personal problems with which corporate America has not previously been involved. And so we are likely to see more corporate investment in daycare, long-term care facilities, continuing education, innovative health-care experiments, and possibly even affortable rental housing. Most companies know that they aren't very good at running enterprises of this sort -- it literally isn't any of their business. And so many are likely to turn to the people who do have a track record: Independent Sector organizations. We see this already in the daycare field, for example, where most of the (admittedly small) corporate investment takes the form of either contracts with non-profit providers or payments to employees that allow them to buy services on their own -- again, usually from non-profits. 2/

So if the economic future is rosy, the Independent Sector should gear up for a flood of demand to help corporations with human service projects, and they should begin planning the most effective ways to do so now. One way to do this is to seek out a few companies that are willing to serve as testing grounds for the development of replicable models. "The company store" of early 20th century "welfare capitalism" may well be replaced by the company grant or contract of welfare capitalism in a new form, and if it is non-profits would do well to be ready.

Now imagine a rosy future on the governmental side. To see what this could be, one need only listen to the statements of the present field of presidential candidates, particularly on the Democratic side. Most of the candidates appear to believe that the nation should develop a more adequate system of health insurance -- a system that would protect the 35 million people now without coverage, pay the cost of catastrophic illness for the elderly and lighten the burden of long-term care. Most also believe that we need to improve the quality of our educational system at all levels, convert welfare programs into jobs programs, help poor children get a better start in life, solve the problems of the homeless, do a better job of protecting the environment and strabilize our shaky financial markets. And opinion polls have repeatedly shown that the overwhelming majority of voters both share these goals and say they are willing to pay substantially more in taxes to achieve them.

If Washington gets back into the business of doing these sorts of things, it is obviously going to need partners, as it has in the past. In the first instance, the partners are likely to be state and local governments. But when it actually comes to service delivery, they in turn will work through Independent Sector organizations, as they always have. Or at least I hope they will. I shudder to think of most public welfare departments, on their own, trying to develop individualized evaluation, training, placement and daycare packages for welfare mothers, as most advocates of "mainstreaming" AFDC recipients think they should. While there are many able people in state and local welfare agencies who understand what is involved in this sort of undertaking, I think that the constraints under which they work would make it very difficult for them to gear up quickly to deliver comprehensive "work-welfare" services on a large scale, as they would probably be required to do, without a great deal of outside help. Likewise, it seems to me that most governmental efforts to shelter the homeless have been far less effective by almost any measure than more modest voluntary sector initiatives.

If, then, we see a revival of federal activism, the Independent Sector should get ready for a truly enormous surge of demand -- because the likely directions of new activism will be heavily weighted in the areas of improved human services in which much of the sector specializes. And, importantly, much of the demand will be to deliver services that nobody today fully understands how to deliver. I have already mentioned mainstreaming welfare mothers and caring for the homeless in appropriate ways. Add to that list developing cost-effective, non-institutional systems of long-term care, establishing more abundant high-quality child nutrition and daycare services, finding mechanisms to provide universal, affordable healthcare services and working with government to fight drug abuse, reduce drop-out rates, upgrade elementary and secondary education and develop better environmental strategies.

In all probability, there is no one best way to do any of these things -- no "cookie cutter" model for the nation as a whole. Different approaches will be effective in different locales. And that is why the Independent Sector is particulary important in a rosy future. The sector is everywhere, it takes many different forms and it often has strong community ties. It should use these advantages to do its homework -- to look for ways to do the things we don't presently know how to do, before the demands of a revived federal government arrive. Otherwise it will be caught unprepared and, once again, face the charge of "voluntary sector failure." More importantly, it will be letting the nation down.

Make up-front investments. Experiment now with progressive states and counties (and there are a lot of them) to find applicable models for the future. And don't just look at service technology. Look too at new management and financial structures, such as chartering non-profit corporations in the areas of daycare, long-term care, health insurance and so forth. Finally, develop improved systems for recruitment, so that you can attract the very best people to your expanded efforts.

The pessimistic scenario. So much for optimism. Now let's face up to another possibility.

Anyone who is paying attention must have very grave doubts about whether this country's economy will, in fact, take off again in the near future and whether the federal government will adopt a progressive agenda. With regard to the former I have little to add to the daily reports on the business pages of any major newspaper: the Reagan recovery has always been artificial in a great many ways, productivity is still lagging, many sectors are still besotted with wasteful speculative activity, foreign competition is still stiff, the financial markerts are suffering from borderline schizophrenia, and so forth.

On the political front, I think we face a cruel paradox. Although most of the candidates are promising a new wave of activism, and although overwhelming majorities of the public support their agenda, no one seems to believe what they say. The present field of presidential contenders seems to be suffering from a credibility gap that could well destroy the possibility that we will have a progressive president and congress -- and, strangely, that gap has little to do with either them or their proposals.

The same polls that show widespread public support for those proposals also show that the public is highly skeptical about the ability of government to deliver on its promises. In other words, ordinary Americans would like to enjoy the benefits of all the new initiatives being discussed, but they have a hard time believing that any those measures can be implemented, at the federal level anyway They apparently find it difficult to imagine an America in which they can count on national government to solve national problems.

This public skepticism means that the more vigorously candidates advocate progressive reforms, the more unrealistic they appear. The public assumes that the more outspoken candidates can't possibly be serious about the bold ideas they are setting forth: they must secretly have in mind some diminished version of what they describe. As a result, there is a temptation for many of the "smart" people on the campaign trail to pull their punches: to lapse into a rhetoric of half-measures and vaguely stated good intentions. There is a lot of talk about "first steps," trade-offs," and "goals," that will be achieved only at some time in the indefinite future.

But the credibility gap that is separating candidates from voters is more than just a cruel twist of fate for those who aspire to be president. It is a gutting of the American political process. What should be the essence of politics in this country -- responding to public needs and aspirations - has become impolitic in this presidential campaign. In the end, that creates an election without meaning: it signifies nothing, it ratifies nothing, it sends no message that would guide or constrain the next president. And the person who can take most credit for this turn of events is none other than Ronald Reagan.

The greatest success of the Reagan presidency was to focus political debate on concerns about the size and scope of government, rather than on questions about its effectiveness in meeting national needs. The president who began his term by declaring that "government is the problem," and then ran up a massive federal deficit to prove his point, propagated two great myths: that big government is inherently a bad thing, and that even if it wasn't bad we couldn't afford it anyway. 3/

This is old stuff from conservatives, and every few decades the nation rediscovers that it simply isn't true. In an increasingly complex and interdependent society, national government must play a large role in securing the general welfare. And big government in the United States has a long string of successes to its credit: greatly reducing poverty among the elderly and other groups, advancing civil rights, making home ownership and higher education possible for tens of millions of people, building and maintaining our national transportation system, promoting science and technology, subsidizing virtually every sector of our economy, and much more. Everyone in the United States benefits enormously from big government, and few Americans would be willing to live without the benefits it confers. Moreover, no one can realistically believe that this country will be able to meet the challenges of the future in areas such as health, education and the environment without the national leadership and resources that only the federal government can provide.

So much for the issue of size. The issue of cost is also illusory. The United States devotes a far smaller portion of its Gross National Product to social programs than most other developed countries do, and there are few economists who believe that devoting somewhat more would harm our national prosperity. Social spending doesn't destroy national wealth; it re-routes it to building a stronger society and economy. Federal deficits are a problem, but most economists believe we can afford to pay for the government we have and to buy somewhat more if we need it to solve our national problems.

But despite the transparent falsehood of Reaganism's two great myths, most politicians and "experts" these days feel obliged to pay homage to the idea that we live in "an era of limited resources." And the same people portray the federal deficit as a stopper to any serious discussion of large new initiatives.

In short, shrouded in a cloud of misunderstanding and distrust, candidates and voters appear to be "faking each other out" this year. And there is a very good chance that the result will be a continuation of the do-nothing politics of the last seven years.

That would be a very great national tragedy. Because the problems that face us today are not just temporary aberrations. They are the result of enormous social and economic changes that are profoundly tranforming the lives of each and every one of us. Changes in the structure of our economy are creating widespread anxiety about job security, skills and incomes. Social changes, such as the entry of women into the workforce, are sending families in search of more adequate systems of daycare, education and long-term care for their elderly parents. America has developed an underclass of several million people, and children raised in that environment will make up a large portion of the workers and citizens of tomorrow. And American society is aging: in the future we will have fewer active workers and more dependent retirees, whose cost to society, particularly in the area of healthcare, is soaring out of sight. 4/

In short, in virtually every area of our social and economic life, this country is on a collision course with the future. But, because of the political confusion this year, there is a good chance that we will not act to avoid the collision very soon.

What happens to the Independent Sector then? What happens to it if a pessimistic scenario on both the economic and political fronts comes true?

If past history is any guide, the sector will suffer, diminish, muddle through, try to fill gaps, speak out, and hope, as it has in recent years. And, as in recent years, it will seek partnerships with progressive industries and state and local governments that are trying to fill the void left by federal inaction.

That is not a wholly gloomy prognosis, but it is certainly not as attractive as the rosy scenario outlined earlier. And in light of the national tragedy that would result from continued federal inaction and economic decline, people who care as much about the future of this nation as much as most people working in the Independent Sector do can hardly be expected to find it acceptable. You have already seen your numbers dwindle and your prestige and influence diminish. You cannot relish the prospect of more of the same.

The sector as movement. Since I do not relish that prospect any more than you do, I would like to propoose an alternative scenario for the Independent Sector, for consideration in case the pessimistic political and economic scenarios come true.

My modest proposal is that the Independent Sector might put the shoe on the other foot. Rather than responding to political and economic developments, it might take the leadership to bring about progressive change. I do not have in mind primarily leadership in small ways, such as supporting progressive organizations, dealing with neglected needs, or funding "alternative organizations" on a case-by-case basis. You already do that; it is eminently worthwhile and I would urge you to continue. What I have in mind is consciousness-raising and action-forcing activities on a larger scale.

For example, looking back over the history of voluntary activities in the United States, it seems to me that there is a great difference between the grange movement, the settlement house movement, the cooperative movement and the trade union movement of late 19th and early 20th century America and most recent Independent Sector activities. They were movements. They were everywhere, they mobilized enormous numbers of people, they tried to solve problems by voluntary action, not just "make a contribution," and inevitably they were breeding grounds for reform politics. Of course, they failed to solve the problems entirely, but their large efforts at the very least forced government to get involved, and they created institutions that continue to be of great importance to our national life. Their reform culture also nurtured future activists, and the approaches they developed through trial and error often proved to be critically important experiments for future state-building developments.

Or if these examples seem too remote from the experience of most of us today, consider another type of movement with which most people in the Independent Sector are intimately familiar. One of Andrew Carnegie's greatest concerns was for the future of school teachers. In particular, he believed that they deserved a decent income in their retirement years. So he set up the Carnegie Foundation (now the Carnegie Foundation for the Advancement of Teaching) for the purpose of providing pensions to not just some, but all retired teachers. That was truly an ambitious effort to solve a problem by volunary effort. And it, too, was a failure in its initial form. Carnegie and his advisors soon realized that no endowed foundation could possibly muster the resources required. So they set up the participant-controlled insurance plan now known as TIAA-CREF, on which many of us are depending for a great part of our retirement income.

Like the grangers, the co-ops, the settlement houses and the unions, TIAA was also a movement, in the sense that it entailed the active involvement of large numbers of people banding together for their mutual benefit. And like those other efforts, it was a self-help movement: it asked something of its members as well as of its sponsors or the public at large.

That was at a time when few companies had private pension plans and long before Social Security. TIAA met a real need. And together with social insurance ideas that another non-profit institution, the University of Wisconsin, developed in working with state government, it served as a model, experiment, and forcing activity for futrure developments in both the public and private sectors. 5/

If the economy falters, and the election proves to be a fizzle in terms of social reform, it is at least worth considering whether Independent Sector organizations should band together in some large scale efforts of this sort. There are some very hopeful recent precidents. The two I know best were initially developed by the Ford

Foundation. They are Mike Sviridoff's Local Initiatives Support Corporation (LISC), dealing with low-income housing problems, and the Manpower Demonstration Research Corporation (MDRC), originally headed by Barbara Blum and now ably led by Judy Gueron, dealing with mainstreaming welfare mothers into the workforce.

It is impossible to exaggerate the importance of MDRC in changing the conventional wisdom in the political world about how welfare programs should be structured. And it is impossible to exaggerate the influence of LISC in the less visible area of housing policy -- let alone the enormous good it has done for thousands of low-income people and their communities. Although supported by foundations, various levels of government and industry, they like earlier movements are based on the idea of self-help: tenant-managed housing, in the case of LISC, and helping people to become self-supporting, in the case of MDRC. I hope that you will all get behind them, and help them to prosper, grow and influence thinking.

There is no danger that the success of such groups will create the impression that government action is unnecessary. Unlike earlier movements, they acknowledge that the problems they are trying to solve are too vast -- they are simply trying to do as much as they can. But the more they do, the more pressure they exert on government -- and on business for that matter -- to act, if for no other reason than that they show skeptical politicians that really complex problems can be solved. Government comes to feel that all it has to do is replicate what such groups are doing on a larger scale. Even if this isn't true, their example at least creates a constituency in government, business and the general public for a reform agenda.

So, if the wost case economic and political scenarios come true, I would suggest that Independent Sector organizations consider banding together in some other large-scale, coordinated "movements" in areas where they can hope to have some impact. The problem of the homeless is an example of an area that commends itself -- because of the enormous public concern it has generated, because it is almost everywhere and because in any particular location fairly small numbers of people are affected.

To take just one case, I am told that in Washington, D.C., where I work, there are 5000 to 6000 homeless people. It seems to me criminal that so small a number of distressed people can't be helped, and helped very well. Estimating the cost of shelter, food, counseling and out-placement for each one of these people at what would have to be a very high number -- poverty level income -- $25 - $30 million would be required. Given the fact that local government already makes a contribution, the cost of a government-voluntary sector partnership that would entirely solve the problem in D.C. would be far less than that. It would be well within the capacity of a consortium of large and small non-profits, particularly with a special fund-raising effort. And, of course, the cost could be reduced if there was more emphasis on self-help, rather than just custodial care: if the more able among the homeless were involved in running the shelters and if the major goals of the effort were to help homeless people either to return to their families or to find better ways of caring for themselves.

I know that many of you already do a lot for the homeless. I am only suggesting that you consider submerging your institutional identities enough to make it or some other problem the priority for a coalition of groups. And the priority should be not just to help, but to solve the problem, to the extent you can, with as much involvement by the general public and the beneficiaries of your actions as possible. Also, I am not suggesting that Independent Sector organizations take permanent responsibility for caring for the homeless. I think that if you took up this charge and succeeded, or at least made a good showing in some major cities, government at every level would feel forced to mount an adequate response.

And, of course, I am only using the homeless as an example, although I think it is a good one. You can pick any one of a great many equally worthy causes around which to organize a movement. And it really doesn't matter which one you pick. Because the important thing is to create a strong and visible impression on the public mind and on the minds of politicians that social problems can and must be solved: forcing action by example.

In this respect, I think that the conservative theory of the Independent Sector is just wrong. Independent sector activism will not and should not replace the need for government and business activism. It never has. The more any one sector leads in addressing major problems, the more likely it is that the others will follow -- and government and business are the greatest copy-cats of all when it comes to human service issues.

Conservatives should know this better than anyone else. The development of the conservative "movement" as an intellectual force in the United States over the last few decades was to a significant extent funded by donations from wealthy individuals and conservative foundations. And that funding entailed not only support for research and writing, but also the development of intellectual networks and the dissemination of ideas. Independent Sector activism on the right fostered a movement that eventually contributed to a major change of direction by government at the national level in this country.

Those of you on the progressive side who are primarily committed to supporting ideas rather than activism can profit by the example of conservative activists. Why don't progressive foundations do more to disseminate progressive ideas? Too often they are content to fund research and writing without taking into account the fact that those products must be aggressively sold in the competitive marketplace of ideas.

I can testify from personal experience, that if you have developed intellectual products -- books, reports, and so forth -- that set forth ideas on the progressive side of the spectrum, there is practically nowhere you can turn to get the type of high-powered public relations assistance you need to bring those ideas to public attention, even if you have the money to pay for it. There is practically nobody in that business. One simple way that organizations devoted to ideas and concerned about the lack of social progress could help to stage a "movement" would be to establish a full-service public relations agency capable of providing a complete menu of assistance at a reasonable cost to their members or grantees

But I do not want to get carried overboard by my personal concerns. There are many ways to instigate movements, and they are valuable and valid undertakings at all points on the political spectrum. In fact, most causes, such as those of the homeless, should provide fertile common ground for Independent Sectror organizations with widely divergent perspectives.

My suggestion is simply this: if political and economic clouds blot out the bright future for the Independent Sector that we all hope for, leaders of the sector should consider mobilizing their efforts to change the climate within which they operate by setting examples on a large scale. And my further suggestion is that if they do, they should make a special effort to involve as many members of the public at large as they possibly can.

NOTES

1. See Solomon, 1985.

2. See Bureau of Labor Statistics, 1988.

3. For a full discussion of these myths and why they are wrong see Chisman and Pifer, 1987, pages 85 - 118.

4. For a full discussion of these and other driving forces that are transforming American life, see Chisman and Pifer, pages 169 - 218. For discussions of all aspects of societal aging, see Pifer and Bronte, 1986.

5. For a discussion of the origins of public and private pension systems, see Stevens, forthcoming, and other essays in Weir, Orloff and Skocpol, forthcoming.

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SECTION THREE:

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SELECTIVE SURVEY RESULTS RELATED TO ACCOUNTABILITY: PRELIMINARY FINDINGS OF A NATIONAL SURVEY

by

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SELECTIVE SURVEY RESULTS RELATED TO ACCOUNTABILITY:
PRELIMINARY FINDINGS OF A NATIONAL SURVEY*
conducted for
PERCEPTIONS OF NONPROFIT ORGANIZATIONAL EFFECTIVENESS STUDY

INTRODUCTION

The study addresses perceptions of nonprofit organizational effectiveness as viewed by national state and local executive directors and chairpersons of boards. There has been little or no comparable study of nonprofit organizational effectiveness done before. The challenge of this paper is to focus on perceptions of effectiveness related to accountability. The term accountability immediately raises the related issue "accountable to whom." Nonprofit organizations are accountable to a board of directors, to their constituencies including: service populations, volunteers, individual financial contributors, staff, external supporters (e.g. foundations, corporations, government), and to the broader community.

The data were collected from a national stratified random sample selected from the IRS file 990. Board chairpersons and executive directors of 2,677 nonprofit organizations were surveyed as to their perceptions of what contributes to the effectiveness of their organizations. In addition, the survey collected descriptive information about the characteristics of the organizations, their management procedures and policies, and the personal background of the chairpersons and executive directors. A supplementary purposive "leadership" sample, consisting of executive directors and board chairpersons of 250 local affiliates of health and welfare organizations was also surveyed to provide a basis for comparison.

Questionnaires were received from 659 executive directors from the national sample and 347 board chairpersons, representing 856 different organizations. From the leadership sample, 88 executive directors and 66 chairpersons returned completed questionnaires.

The findings are divided into four parts that serve as a framework for exploring the data related to accountability. This paper will selectively highlight items in the four categories mentioned that may prove to be significant in more definitive analysis of data. They are: 1) descriptive, 2) perceptual, 3) interrelationships and 4) organizational and control practices.

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* The survey is part of a larger multi phase study which is still in progress (see appendix). It would be premature to attempt any definitive analysis.

I. **DESCRIPTIVE DATA**

The formal characteristics of an organization such as its revenue sources and governance structures, help define the accountability mechanisms of nonprofit organizations. The survey elicited factual data on these dimensions and disclosed some significant patterns across the spectrum of these organizations.

Revenue Sources

Executive directors were asked their sources of revenue. Over 80% report they receive income from individual donations, with progressively smaller percentages reporting income from corporation gifts, foundation gifts, government grants, fees from service recipients, membership dues and endowment/investment income (see Table 1 below). Indirectly Table 1 indicates the revenue based constituencies to whom nonprofit organizations are accountable.

Table 1	Receives income from each source	Average % of 1986 income from each source
Individual donations	83*	17%
Gifts from corporations	70	4
Gifts from foundations	66	4
Government grants	66	17
Fees from service recipients	64	16
Membership dues	62	10
Endowment/investment income	59	5
Personal bequests	51	1
Fees from third party payors	50	6
All other sources	67	18

Five Year Trend in Revenue

A little more than half the executive directors (national sample) report their organizations are increasingly receiving income from individual donations and fees from service recipients. Over 65% report decreased income from personal bequests, fees from third party payors, foundation gifts, corporate gifts, and government grants. Over half also report decreased income from endowment/investment income and from membership dues. In other words, increases in revenue are the result of those most directly associated (clients and individual donors) with the organization.

Board of Directors

Almost half, (47%) have a formal policy regarding the board's composition and 28% an informal policy, compared with 25% who do not have a policy. These policies differ considerably. Frequently named provisions included: geographic dispersion, representation from religious, racial/ethnic groups, organization members, and occupational backgrounds. Twelve percent have policies about ethnic, racial or gender involvement. Over three-fourths 79%) do not have a policy excluding individuals because of possible conflict of interest.

Of telling importance to the theme of accountability is that constituencies which are served by an organization are represented on its board. Fifty-six percent of boards have half or more of their members from the constituency served and 57% have half or more from the general community, compared to 42% from private business and 26% from professionals.

Most organizations make appreciable time demands on board members. Moreover, 57% have monthly board meetings, 12% meet every two months, 15% quarterly, 10% semi-annually or annually, and 7% have some other meeting schedule.

Activities of the Board of Directors

The board as the center of governance serves as the closest linkage between the ongoing operations of an organization and its many constituencies.

From the chairperson's perspective, the large majority of boards of directors work jointly with executive directors. In 78% of the organizations, the board's relationship to the executive director is that of a "joint problem solver," as a reactor in 15%, and as an initiator in 8%.

Boards of directors are most likely to participate actively in financial matters (budgeting and fundraising) and in general organization matters (organization planning and the Executive Director's annual review). They are least likely to participate actively with respect to staffing and program implementation.

Chairpersons are more likely than board members to participate actively in all aspects of an organization. They are especially likely to participate actively in organization planning and fundraising. Activities that represent the organization to the public, such as speaking, advocacy, and other community relations also rank high among those in which chairpersons participate actively.

Chairpersons, over a three-month period, reported spending an average of 57 5 hours on organization activities, 26.9 hours working with the executive director, 13.9 hours in conversation with board members regarding organization business 8.5 hours at board meetings, d 8.2 hours at committee meetings.

In summary, revenue sources, trends in revenue, composition of boards, and activities of boards of directors are perceived as related to accountability and lead to increased nonprofit organizational effectiveness.

II. PERCEPTUAL DATA

Beyond these factual dimensions, perceptions of effectiveness can enlighten aspects of accountability. How effectively an organization performs is an indicator of its accountability to its mission and to its constituency. Effective management connotes the ability to manage efficiently, legally and responsibly.

Chairpersons and executive directors were asked to rate how effective their organizations are with respect to fifteen specific attributes. The percentage of chairpersons and executive directors that rated their organization as above average in effectiveness is in almost all cases very close.

Seventy-three percent of chairpersons and 70% of the executive directors rated their organization above average with respect to carrying out its mission. Sixty-seven percent of both categories rated their organizations above average in providing mission-related quality services. About half gave an above average rating with respect to efficient administration and financial management.

The close correspondence of ratings given by chairpersons and executive directors on thirteen of the fifteen attributes reveals that both internal staff and volunteer board chair have similar perceptions of the organization, lending a degree of credibility to the statements.

Characteristics that influence effectiveness

To provide insight into the ratings of organization effectiveness, chairpersons and executive directors were asked open-ended questions about the performance characteristics that make for, and that detract from, the effectiveness of non-profit organizations. The responses of chairpersons and executive directors tended to parallel each other. However, there were some important differences in the responses of those in the leadership sample. The most salient factor mentioned was mission, a factor that indirectly addressed organizational accountability.

Mission related characteristics (e.g., clarity of goals, quality of program, caring about goals) were named by chairpersons and executive directors in both the national and leadership samples. Management characteristics rank next in frequency of mention, while board related characteristics were named by only a small minority.

Chairpersons in the leadership sample were particularly likely to refer to leadership and to the board. They were relatively unlikely to refer to staff and to intra-organization relations.

Executive directors in the leadership sample were more likely than those in the national sample to refer to leadership and to outside relations, and relatively likely to management, staff, and the board.

Table 2

	Named as making for effectiveness by:			
	Executive directors		Chairpersons	
	National	Leadership	National	Leadership
Mission	64%	67%	53%	74%
Management	42	53	32	48
Intra-org. relations	26	29	29	20
Staff	23	30	28	15
Leadership	18	30	16	24
Outside relations	19	32	20	24
Board	10	16	8	13

Note: Most respondents named more than one influence.

Three factors were named by large percentages as detracting from effectiveness -- mission-related qualities (such as lack of purpose, ineffective program, and being out of touch), weak individual motivations, and poor management practices. Once again mission proves salient.

The analysis of perceptual data seems to indicate that mission is a dominant factor in determining characteristics that influence organizational effectiveness. If the mission is properly defined then the organization is perceived to be effective.

III. CHALLENGES/INTERRELATIONSHIP DATA

In probing for what influences effectiveness, the survey identified a number of key ingredients that affect accountability to the organization's mission and service constituencies.

Fundraising

Looking ahead for the next three to five years, fundraising is the overriding concern of executive directors. When presented with a list of six types of concerns (raising funds, retaining good staff, building constituency, recruiting good staff, defining program, recruiting corporate leadership) two-thirds of executive directors selected fundraising as one of the two most pressing challenges for themselves and their organizations over the next three to five years in working to achieve their missions. Staff concerns and constituency relations, which rank next in frequency of selection, are secondary concerns in relation to fundraising. Moreover, fundraising stands out as a pressing challenge.

Priorities for achieving maximum effectiveness

Both chairpersons and executive directors were asked to rate the contribution of twelve practices (e.g. emphasize quality of service in relation to mission, give primary consideration to mission in all decision making, develop team concept to task performance, etc.) to achieving maximum organization effectiveness. For this purpose, they rated whether each practice should be assigned the "highest priority," whether it should be considered important but not the highest, useful but not necessary, or a low priority.

Among both chairpersons and executive directors, the highest ranking factor with strongest support (66 to 83%) is to emphasize the quality of service in relation to mission. Giving primary consideration to mission in all decision making is the next highest priority. A third priority was to develop a team concept. Executive directors in the leadership sample were more likely than executive directors in the national sample, and more likely than chairpersons in both samples, to assign the highest priority to developing a team concept.

Accounting for differences in effectiveness

Chairpersons and executive directors were also asked to rate the significance of nine factors (e.g., goals and objectives are formulated in direct relation to mission statement; building a team among the board and staff has high priority; a formal statement of the organization's mission has been formulated) as possible explanations of why some organizations are more effective than others. Each factor was rated as "highest significance," "significant but not highest," "useful but not necessary," and "not at all significant."

A strong mission orientation and the development of a team approach that integrates and dedicates the board of directors into the organization and its mission are the most significant factors in organizational effectiveness.

When the nine factors (see Table 3) are ranked in terms of the percentage that rated each as having the highest significance, with a few exceptions, the rank order is very similar for chairpersons and executive directors in both the national and leadership samples. Large majorities of all four groups think that formulating goals and objectives in direct relation to a mission statement and having a formal statement of the organization's mission are of the highest significance.

Majorities in all four groups also assign the highest significance to building a team among board and staff and an annual recommitment of the board of directors to shared goals and objectives.

Table 3 Proportion that felt each practice has the "highest significance" as an explanation of why some organizations are effective

	Executive directors		Chairpersons	
	National	Leadership	National	Chairpersons
Goals and objectives are formulated in direct relation to a mission statement	64%	80%	69%	75%
Building a team among the board and staff has high priority	56	60	63	63
A formal statement of the organization's mission has been formulated	55	65	59	60
Board of directors annually re-commits to shared goals and objectives	53	62	54	52

Table 3
(continued)

Proportion that felt each practice has the "highest significance" as an explanation of why some organizations are effective

	Executive Directors		Chairpersons	
	National	Leadership	National	Chairpersons
Priority is given to constituency needs when using resources	44%	58%	49%	64%
Attracting resources is a priority objective	46	65	45	70
Building staff capacity to recruit and train volunteers	32	45	44	41
Procedures have been developed to plan for and evaluate resources	26	46	33	45
Financial resources are used strictly according to budgets and are not considered interchangeable	12	8	25	30

The two most frequently named factors by executive directors in the national and leadership samples are board (42% and 50% respectively) (supportive cooperative and concerned) and a good staff (34% and 50%).

Also named relatively often as necessary for effectiveness by executive directors were their personal traits (determination and patience, being people oriented, ability to communicate, energy, and flexibility), their management skills, and their relations with the outside community.

Chairpersons were asked what priority they would assign to each of fifteen qualities as ways of judging the effectiveness of an executive director. A strong commitment to the organization's mission stands out as the single most important criterion that chairpersons would use (National sample 82% and Leadership sample 85%).

Conflict resolution

Chairpersons and executive directors were asked to think of some recent conflict, naming the source of the conflict, who was involved, and how it was resolved.

Chairpersons and executive directors cited similar types of conflict. The most frequently named had to do with personal conflicts, resources, goals and objectives, and questions of authority.

When conflicts arise, they are more likely to be resolved through compromise or consensus than through a unilateral decision. Thirty-four percent of the chairpersons and 47% of the executive directors perceived conflict to be resolved in this manner. In most cases, resolution was achieved by the opposing groups achieving a consensus or compromise or by the board of directors making a decision. Undoubtedly related to the different mix of persons involved in conflicts referred to by chairpersons and executive directors, chairpersons were more likely to report that resolution was achieved by the board and executive directors by consensus or compromise achieved by the involved parties.

Important motivations for retaining professional staff

Chairpersons rated the importance of seven factors as motivations for retaining executive directors and senior professional staff.

With respect to retaining executive directors, close relations with the Board was the most important motivation by far. The two next most important factors were independent decision making and the result of periodic performance or salary reviews.

A different pattern emerges regarding very important motivations for retaining senior professional staff. Periodic performance and salary reviews was rated very important by a large majority of chairpersons in the national sample (70%) and independent decision making by a smaller majority (58%). Two other factors -- close relations with the board of directors and fringe benefits -- were rated very important by just under half.

In summary, fundraising is the most pressing challenge of nonprofit organizations. Centrality of mission -- in decision making, the quality of service, formulating goals and objectives, and leadership of the executive director -- is perceived to play a key role in contributing to the accountability and effectiveness of nonprofit organizations. Other priorities in ach eving effectiveness were to develop a team concept and to resolve conflict through compromise or consensus. While close relations with the Board was key to retaining the executive director, periodic performance or salary review and independent decision making were important factors in retaining all senior level staff.

IV. ORGANIZATIONAL/CONTROL PRACTICE DATA

More generally, these findings give substantive meaning to the concept of effectiveness with emphasis on fulfillment of mission and responsiveness to constituency. These are the prerequisites of accountability. How they are institutionalized within organizations and activated in their recurrent opeerations was further clarified by the survey results on committee activities, leadership practices, oversight activities as well as, internal communications.

Committee activities

Ninety percent have standing committees other than an executive committee and 47% have advisory committees. The most common types of standing committees are Financial (75%) and Nominating (72%). Also relatively common are Program (52%) and Development(42%), while only 15% have a Personnel committee. Over half the organizations have volunteers other than board members who serve on standing or advisory committees. These committees serve as bridges between constituencies and organizational operations and shape the activities that implement the missions of nonprofit organizations.

Leadership practices

Among both chairpersons and executive directors, giving primary consideration to the organization's mission in all decision making and emphasizing quality of service in relation to mission rank most highly as ways of achieving maximum effectiveness. Developing a team concept has a somewhat lower priority among both.

Sizable, though smaller, proportions of chairpersons and executive directors in both samples assigned the highest priority to external public relations, board involvement in the organization and its operations, maintaining formal systems of monitoring and evaluating operations, stressing management efficiency, and setting accountability guidelines.

Two factors were named by large majorities of chairpersons and executive directors in the leadership sample as having the highest significance, and by almost half of those in the national sample -- making a priority objective the attracting of resources and giving priority to constituency needs when using resources.

Close to half of chairpersons and executive directors think building staff capacity to recruit and train volunteers is important. A similar pattern exists with respect to developing procedures for planning and evaluating resources.

The most frequently mentioned aid to effective performance of duties was an effective staff. (Chairpersons - 41% national sample and 80% leadership sample; Executive Directors 34% and 50% respectively). Among chairpersons, effective boards and effective staff (mostly executive directors) were named most frequently.

Characteristics that were named most often needed by effective executive directors were strength of leadership, and interpersonal skills. Other characteristics named relatively frequently relate to management skills, inspirational qualities, techniques of leadership, and personal abilities and skills.

A strong mission orientation stands out once again, as the single most important criterion that chairpersons would use in judging the effectiveness of executive directors.

Relations with the board of directors, establishing clear lines of authority and responsibility, ability to represent the organization to the public, and expertise in substantive areas also rank high as criteria for judging effectiveness. These are essential elements for assuring accountability.

Oversight activities

Traditionally a prerequisite for organizational accountability is a formal system for monitoring and evaluating organization activities. These have become widely established in both principle and practice. Only among organizations that are rated low in effectiveness by their executive directors is the absence of such systems common.

Among chairpersons in the national sample, 58% said it is very important to have a monitoring and evaluating system and 29% said it is fairly important, while only 13% maintained it is not too or not at all important. Among chairperson in the leadership sample, 77% said such systems are very important, 20% fairly important, and a mere 3% not too or not at all important.

Seventy two percent of executive directors in the national sample, and 98% of those in the leadership sample, report their organization have a monitoring and reporting system. Of the organizations that were rated very much above average in effectiveness, 80% have such a system, compared with 59% of organizations that were rated average or below average.

If an organization has a system for monitoring and evaluating organization activities, the executive director is almost certain to be involved (80%). Boards of directors are also likely to be involved (69%) and program staffs slightly less so (64%). Of the leadership sample, in 94% of the organizations that have a system program staff is involved, compared with 92% in which the executive director is involved and 74% in which the board of directors is involved.
A number of other oversight practices are also common, while others have been adopted less frequently. Periodic reviews and revisions of long-term plans and strategies are virtually universal, while audits by outside accounting firms are utilized by the overwhelming majority. Large majorities also have a formal system in place to guide organizational programs and activities, issue annual reports available on request to the public, and regularly evaluate the cost-efficiency of fundraising. Formal guidelines concerning acceptable and unacceptable fundraising techniques are the least common. Larger proportions of the organizations in the leadership sample than of those in the national sample, have such guidelines.

Intra-organization communications

More informally, communication serves to explore not only how effectively an organization performs but also how accountable it is in translating mission into operations and serving constituencies.

Communications between chairperson and executive directors tend to be frequent. About half (49%) of chairpersons in the national sample meet or talk with their executive directors more than once a week, 21% about once a week, 17% two or three times a month, 8% about once a month, and 5% less often. There is little difference in this respect between organizations that were rated very favorably in effectiveness by their chairperson and those that were rated less favorably.

Most chairpersons and executive directors communicate with each other at least once a week. Communication between staff and board members is reported to be somewhat less frequent. Chairpersons are more likely than executive directors to think that communication between staff and board members is frequent and that it is an important contributor to an organization's effectiveness.

Board committee activities, leadership practices by executive directors and chairpersons, oversight activities and intra-organization communications seem to have a great bearing on accountability and thus organizational effectiveness as perceived by executive directors and board chairpersons.

SUMMARY

The overall findings define organizational effectiveness as perceived by executive directors and board chairpersons. Effectiveness in this context provides an operational yard stick for accountability. The findings therefore, clarify how accountability is served through organizational governance, leadership, management and activities.

Since this is a preliminary review of the survey findings and additional findings are being collected, no overall conclusions can be drawn at this time. However, we can observe that the accountability of nonprofit organizations involves very complex processes and that these processes can significantly influence the effectiveness of those organizations.

In summary, the findings of the study suggest that centrality of mission stands out as the most important criterion in judging accountability and effectiveness of every facet of a nonprofit organization in the perception of board chairpersons and executive directors. When mission is the dominant factor -- in goal setting, program development, decision-making, resource development, response to constituency, quality of service and the orientation of the executive director and board members -- a nonprofit organization is perceived to be effective.

The most pressing challenge facing nonprofit organizations is fundraising. The two priority objectives for most organizations are 1) attracting resources and 2) giving priority to constituency needs when using resources. It is significant to note that more than half of the executive directors reported that increases in revenue are the result of those directly associated with the organization (clients and individual donors). Service recipients and individual donors are increasingly becoming the dominant revenue based constituencies to whom nonprofit organizations are accountable.

The third priority for achieving effectiveness was to develop a team concept. Factors needed in order to retain the team were independent decision-making (decentralized control) and periodic performance or salary reviews. Included in the team concept was the need for a committed and supportive board and an executive director committed to the mission with strong leadership and interpersonal relationship skills.

APPENDIX

SURVEY OF PERCEPTIONS OF NONPROFIT ORGANIZATIONAL EFFECTIVENESS

I. BACKGROUND

Based on a restricted universe of 1.2 million organizations filed with the U.S. Department of Treasury, the independent sector makes up more than 4 percent of all private and government entities. It contributes 5.5 percent to the national income. The wage and salary component of the independent sector exceeds 7 percent of total earnings from work while employment in the sector (including volunteer equivalents) approaches 10 percent of all employment in the U.S. The annual source of funds available to the nonprofit sector in 1984 totalled more than $250 billion.

Despite the magnitude and importance of the American nonprofit sector, many nonprofit organizations are in trouble. They are struggling to adjust to societal changes that affect their goals and services, and they are under pressure to do more when support from public funds is declining. The future of nonprofit organizations as they struggle to overcome challenges will be directly related to how effectively they are led and managed.

Recognizing this fact, the Effective Sector Leadership/Management Advisory Committee established a subcommittee in 1985 to study "Perceptions of Nonprofit Organizational Effectiveness."

The objectives are to:

- identify the basic factors that relate to effectiveness in nonprofit organizations;
- identify the personal attributes, job skills and experience most likely to produce effective staff leaders;
- identify attributes of boards that contribute to their effectiveness; and
- identify a basic body of literature related to nonprofit effectiveness.

The research plan has four stages:

1) a literature review, that has been completed;

2) a focus group, a select number of nonprofit organization leaders, management auditors and consultants conducted in May 1986 that addressed the questions: What is organizational effectiveness in nonprofit organizations? How can it be described and replicated? (A report of that session is included in the Early Stage Discussion Paper);

3) A quantitative survey, now in process, of a representative sample of nonprofit organizations; and

4) A complimentary qualitative study that will profile 10 nonprofit organizations (to be conducted during 1988).

Design of the survey (on which paper on accountability was drawn)
Board chairpersons and executive directors of voluntary nonprofit organizations were queried as to their perceptions as to what contributes to the effectiveness of their organizations. The survey also collected descriptive information about the characteristics of the organizations, their management procedures and policies, and the personal backgrounds of their chairpersons and their executive directors.

Two questionnaires were developed, one to be completed by chairpersons and the other by executive directors.

The overall structure of the two questionnaires are similar and, where appropriate, identical questions were asked in both questionnaires.

a. Descriptions of the organization (both questionnaires).

b. Characteristics of the board of directors (chairpersons only).

c. Activities of the board of directors (chairpersons only).

d. Personal background (both questionnaires).

e. Personnel recruitment and administration (both questionnaires).

f. Management practices and policies (both questionnaires).

g. Assessing effectiveness (both questionnaires).

A national probability sample of voluntary, nonprofit organizations was drawn from the IRS file 990. The list was stratified by state and by organization function before the sample was drawn. The appropriate questionnaire was sent to both the chairperson and executive director of each selected organization.

A supplementary purposive "leadership" sample. consisting of local affiliates of health and welfare organizations identified by the National Assemby as "effective" was also surveyed. The responses of the chairpersons and executive directors of these organizations provide a point of comparison for evaluating the results of the national sample. However, given the purposive selection method that was need, the leadership sample cannot be considered a representative sample of all voluntary nonprofit organizations.

Potomac Survey Research mailed the questionnaires, conducted follow-up mailings and telephone calls to those who had initially failed to return completed questionnaires, data-entered the responses, and tabulated the results.

Questionnaires were mailed to both the chairperson and executive director of 4,500 organizations that were in the initial national. Many were returned as undeliverable. Also when telephone follow-ups were attempted with organizations from whom no questionnaire was returned, many were unlocatable. This reduced the effective national sample to 2,677 organizations. The leadership sample consisted of 250 organizations and questionnaires were mailed to the chairperson and executive director of each.

Questionnaires were returned from 659 executive directors from the national sample and 347 chairpersons, representing 856 different organizations. While in many cases a questionnaire was returned by only an organization's executive director or by only its chairperson, in 152 instances, questionnaires were returned by both. For that part of the sample, therefore, it is possible to compare directly the replies of executive directors and chairpersons of the same organizations. Also, completed questionnaires were returned by 88 executive directors and 66 chairpersons from the leadership sample.

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Madeleine Green, Director, Center for Leadership Development
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MANAGEMENT AND RESPONSIBILITY IN THE NONPROFIT SECTOR

by

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Like the man who tried to study philosophy but found that humor kept breaking through, Americans sincerely try to practice business and politics as usual but are regularly smitten with an attack of ethics. Now seems such a moment. In politics Gary Hart, who followed a little too closely the example of John F. Kennedy, is held up for blame. In business Ivan Boesky and others trudge off to country club prisons. In religion Jim Bakker earns the scarlet letter. In the movie "Wall Street," bad guy Gordon Gekko preaches and practices greed, while in the movie "Broadcast News," good girl Jane Craig refuses to come out and play with the handsome anchorman because he shed an artificial tear on camera. Ethics is bursting out all over.

The study of business ethics alone is clearly a growth industry. A recent bibliography listed 1,500 references on the subject. Articles and panels on government ethics abound. Governor Cuomo recently put at the top of his legislative agenda the ethics-in-government issue, always an interesting topic in New York state. But what about the nonprofit sector? Are we once again running a distant third? Don't we have scandals as juicy as their scandals? Is the third sector also the MORAL sector, so that we don't have a big problem? Does corporate social responsibility also apply to nonprofit corporations? Having raised these questions, I am not so foolhardy as to try to answer them; I will, however, address the more modest but hopefully still important question of the ethical dimensions of managerial roles in the nonprofit sector. To do this I will use the concept of "responsibility," which unlike "accountability" and other synonyms has a long and rich tradition in philosophical and religious as well as management literature. The word itself is etymologically very significant in this context: "responsibility" comes from the Latin verb spondere, which means "to promise solemnly, to pledge, to vow." This Latin verb is also the root of the English "spouse." The word "responsibility" connotes more than an administrative relationship; it suggests some element of the relationship that we commonly associate with families, friends, clubs, kinship groups, political causes, and religious organizations. The idea that there is "responsibility" in all forms of management, and that this responsibility not only has administrative, legal, financial, and technical aspects but also includes a quasi-sacred trust, is essential to the argument of this paper.

It is important that we base our exploration of this topic on more general studies of organizations and management, as well as on the philosophical and ethical literature on responsibility. Although nonprofits are often seen as a special case because of their frequent ideological, moral, and religious goals, separating them too much from other organizations could blind us to the fact that there is a moral dimension of management and organizations generally. Treating nonprofits as totally different, far from strengthening the case for management responsibility in the nonprofit sector, in my opinion actually makes it weaker. Nonprofit managers do not have moral responsibility primarily because their organizations are religious or humane; they have responsibility primarily because they are managers.

Perhaps still the best articulation of this point is Chester Barnard's famous chapter on "The Nature of Executive Responsibility" in his Functions of the Executive, a book which celebrates its 50th anniversary this year. Barnard, who was a corporation executive and was writing primarily though not by any means exclusively about business management, made the remarkable statement concerning executive leadership, "This general executive process is not intellectual in its important aspect; it is aesthetic and moral."[1] He saw leadership as "the power of individuals to inspire cooperative personal decision by creating faith,"[2] and said that leadership had two dimensions: "individual superiority" which is "the technical aspect of leadership,"[3] and "responsibility," which is "the capacity . . of being firmly governed by moral codes" in the presence of strong contrary impulses, desires, or interests.[4] Responsibility connotes dependability, reliability, character. Executive responsibility is related to longevity of organizational life:

> Organizations endure . . . in proportion to the breadth of the morality by which they are governed. This is only to say that foresight, long purposes, high ideals, are the basis for the persistence of cooperation.[5]

Even in a for-profit organization, cooperative action depends vitally on a complex of "moral" factors including not only the classical prohibitions against lying, stealing, drunkenness, and adultery (read "sexual harassment"?), but also such simple and basic "moral" imperatives as doing something well for the sake of doing it well.[6] Barnard gives the following example:

> Mr. A, a citizen of Massachusetts, a member of the Baptist Church, having a father and mother living, and a wife and two children, is an expert machinist employed at a pump station of an important water system. For simplicity's sake we omit further description. We impute to him several moral codes: Christian ethics, the patriotic code of the citizen, a code of family obligations, a code as an expert machinist, a code derived from the organization engaged in the operation of the water system . . . . He is . . . a very responsible man. It not only takes extraordinary pressure to make him violate any of his codes, but when faced with such pressure he makes great effort to find some solution that is compatible with all of them . . . .[7]

Far from being irrelevant to ordinary work, moral codes and responsibility are central to it. Further, morality and responsibility are central to the task of inspiring and guiding cooperative action, which is the special job of the executive. Barnard's argument throughout the book is that certain functions like planning and decision-making permeate an organization, and that the executive specializes in these functions rather than performing them alone. Likewise, moral codes and responsibility permeate an organization, and there really are, as he says, even moral codes like "devotion to the water system . . . . [O]rganizations depend greatly upon such moral codes."[8] The essence of the executive role, according to Barnard, consists of exercising the function of responsibility, specializing in the phenomenon of responsibility that permeates the organization. Since the effectiveness of an executive depends completely on the extent to which subordinates choose to accept his/her authority, and since that acceptance and the resultant cooperative action rests on, among other things, a complex set of moral codes--one of which may even be "a code of morals derived from the organization"[9]--an executive who is unaware of or unresponsive to these moral codes cannot ultimately be effective.

The leader must not only recognize and respond to but also create morality within an organization: "The distinguishing mark of the executive responsibility is that it requires not merely conformance to a complex code of morals but also the creation of moral codes for others."[10] This includes building "morale," fostering loyalty, creating conviction, and establishing "the morality of standards of workmanship."[11] This creative function is critical: ". . . the creation of organization morality is the spirit that overcomes the centrifugal forces of individual interests or motives."[12]

We instinctively recognize and comprehend this organizational principle in practice. Richard Nixon resigned from the most powerful executive position in the world not for legal or financial or technical reasons but because he had lost moral authority. The nation he led was no longer willing to follow him. He was no longer "responsible," he had betrayed the sacred trust. Recent events in all three sectors have given us examples of people whose executive careers have come crashing down because they got failing grades in "responsibility." They failed not in the technical but in the moral dimension of leadership. The case of Apple Computer is an especially intriguing one. Remember that Steve Jobs persuaded John Sculley to take the CEO position largely on "moral" grounds: the opportunity to change the world by playing a leading role in the societal renaissance of the personal computer movement, as compared with the prospect of selling sugared, colored water (Pepsi-Cola) the rest of his life. Then, with the inexorability of a Greek drama, Steve Jobs himself lost his position because of a failure in moral leadership: arrogance, frequent tirades, and--not insignificantly--treating the Macintosh people better than the Apple II people, i.e., not being fair.

Even the Mafia is an organization whose leaders are motivated by responsibility as well as technical proficiency. This was brilliantly illustrated in the film "Godfather II," in which the young godfather Michael Corleone was so responsible to the Mafia's moral code and so responsible for "the family" that he had his own brother murdered. As Barnard had noted, "High responsibility there must be even in the lowest, the most immoral, organizations . . . ."[13]

Peter Drucker is fond of saying that the practice of management in complex organizations is at least as old as the pyramids. The building of the pyramids is actually quite a good example of the management responsibility issue. On the one hand we are struck by the technical genius of that management process; and on the other hand we abhor the moral aspect of the process, specifically the cruel treatment of the Jewish laborers. But note that in Egyptian theology the managers of the pyramid projects were acting with great responsibility and morality, since they were honoring the divine pharaohs. Those managers were highly responsible in that they got the job done, fulfilled the objectives of the Egyptian nation, and satisfied the gods, who conveniently were their immediate superiors. Far from disproving Barnard's thesis about morality being key to the executive role, the pyramid example shows that these managers were simply following a very different moral code. The issue of management and responsibility is an age-old issue which is continually re-defined as social, moral, philosophical, and religious positions change.

We should add, "and as management theory changes." The classic and wonderfully funny example is, of course, the experiment at Western Electric's Hawthorne plant, where the experimenters found to their amazement that productivity went up when lighting intensity was increased and then went up again when lighting intensity was lowered. Their final conclusion was that productivity had nothing whatever to do with raising or lowering the lighting intensity but had everything to do with how much the workers were noticed, fussed over, and valued. This conclusion (please pardon) electrified the world of management theory, and led us out of the darkness of "scientific management" into the light of the "human relations" school. A new definition of management responsibility, a new moral code, had emerged: managers were to attend to the personal goals of the workers as well as to organizational goals. The superficial reason was higher productivity, but as Barnard and others saw, the deeper reason was that the moral dimension was central to the administrative role: one could not fully understand either management or organizations without understanding the moral dynamics thereof. It is, I think, also worth noting that this most profound of ethical changes in management theory preceded by about half a century the widespread introduction of "business ethics" courses in business and management schools. Such courses are important, but morality, ethics, and responsibility are on much stronger ground when people realize that they are fundamental to understanding and practicing good management, and that they are not simply tacked onto an organization (business, government, or whatever) because they are nice or because they are required by public opinion. Too many homiletic discussions of leadership and values implicitly assume that there can be true leadership without values; with friends like this, who needs enemies? The strongest case for management ethics is the "intrinsicist" argument that the moral factor, responsibility, flows from the very nature of management and organizational behavior.

What, then, can one say about management and responsibility in the nonprofit sector?

It follows from the above that managers in the private nonprofit sector must, like all managers, be specialists in the phenomenon of responsibility which permeates any organization. They must provide not only technical leadership but must create and sustain a "moral" climate which supports the responsible and moral decisions of people within the organization whose cooperative action makes the organization work. As we shall see in a moment, the types of people who work in nonprofits, the kinds of clients nonprofits serve, and the mission and goals of many nonprofits, create a situation in which managers are constantly called upon to exercise "responsibility, the moral aspect of leadership." But note that even the technical dimension of leadership is also "moral" in some sense. The immediate and specific task of the nonprofit or any other manager is getting the job done with a reasonable amount of resources in a reasonable period of time within a reasonably peaceful and constructive environment. Sometimes there is a temptation to excuse some nonprofits from this first commandment of management. Particularly subject to temptation are smaller nonprofits, heavily "do-good" nonprofits, and nonprofits with strongly religious or moral goals. Most people examine such organizations less rigorously and more sympathetically than they would a private hospital or university or research agency, to say nothing of mutual benefit nonprofits such as trade associations, membership clubs, and unions. But special dispensations are not in order for small, do-good, or religious nonprofits; quite the contrary, as we shall see. For all organizations the basic managerial morality is essentially the same. The primary responsibility of a hospital manager is to facilitate the working of the organization so that sick people can get well. The primary responsibility of a college president is to establish and maintain conditions conducive to student learning and faculty teaching, research, and service. The manager must make sure that the objectives of the organization are satisfactorily achieved. That is not simply a technical issue; it is an issue of moral responsibility.

Some years ago, when I was working with a variety of private schools, many of which were religious, I was struck by the fact that a school is or should be, as Bruno Bettelheim would say, a sacred place, because of the powerful and profound things that happen to children and young people within them; and that this is antecedent to the question of whether a school defines itself as religious or not. A school, any school, is a sacred place; and anyone who doesn't understand this shouldn't be running a school or teaching in a school.

More generally, the fundamental reality of a nonprofit organization creates its own morality, and the first responsibility of the manager is to follow that moral code by successfully implementing the goals of the organization. Morally responsible nonprofit managers are not primarily those who avoid fooling around with the church secretary but those who lead the organization to accomplishing its goals, whether those goals are to provide shelter for the homeless or to provide courageous excursions into modern dance. The "promise, pledge, and vow" of responsibility is above all to do well what one is supposed to do as the leader of that particular organization.

I think it is when and only when we get beyond that point that management responsibility in the nonprofit sector starts to emerge as a somewhat distinct form. Nonprofit organizations are clearly different from other organizations with respect to the types of people employed and the number and types of unpaid workers in these organizations. We know that individuals freely join organizations, including work-for-pay organizations, for a rich variety of reasons, including but not by any means limited to (even in work-for-pay organizations) making money. We further know that, up to a certain point, the degree to which an organization satisfies its members' personal goals will determine how successful the organization is in meeting its organizational goals. Nonprofit organizations have unique opportunities and challenges in meeting employee and volunteer goals. Nonprofits are almost exclusively service-producing, labor-intensive organizations. Nonprofits are people industries: they are industries almost exclusively of, by, and for people. Further, the people who work in these nonprofit firms are on the whole unusually well-educated as compared with workers in the other two sectors.[14] This is a function of the type of work most nonprofits are engaged in, which tends to be heavily concentrated in the professional services. So nonprofits are not only people industries; they are much more likely to be inhabited by educated and professional people than are other service industries like fast-food restaurants and travel agencies. The characteristics of workers in the nonprofit field would seem to call for unique types of management responsibility. Social agency directors, heads of advocacy organizations, and opera company managers understand well that their workers cannot be treated in a high-handed, insensitive fashion; whereas managers in a fast-food restaurant or a cannery might be more able to get away with such behavior. The more positive way to say this is that the manager of a typical nonprofit organization faces more complex responsibility toward his or her workers simply because those workers are themselves capable of so much more responsibility, humanly and professionally and educationally speaking, than the typical gas station attendant.

One can further argue that many nonprofits have missions so directly and intimately involved with ethical, moral, and social purposes that the management of these organizations necessarily demands a more explicit form of responsibility than do other organizations. David Mamet's play, "Glengarry Glen Ross," dealt with the ethics of a hard-sell real estate office in Chicago. I'm sure realtors are no more comfortable with this play than ministers are with "Elmer Gantry," but I hope it will not be terribly offensive to realtors if I express the opinion that managing a real estate operation does not demand the same type of moral responsibility that managing a religious institution does. Certainly the reason why the Jim Bakker-Jessica Hahn affair was so shocking or ludicrous, depending on your point of view, was precisely the fact that Jim Bakker had freely taken upon himself a certain level and type of responsibility, that of an ordained minister, a television preacher, and the manager of a large religious organization. We expect certain things of people in his role, and rightly so. The mission of the organization shapes managerial responsibility.

Advocacy organizations also illustrate this point well. As many historians have noted, abolition was the first great secular religious movement in the American experience. Slavery was a burning moral, ethical, and societal issue, one in which the churches were little involved, and when they were it was usually on the wrong side. The movement was carried by moralists, as was the child welfare movement, the labor movement, the mental health care movement, and the women's suffrage movement, all events of the enormous social creativity of the 19th century. The counterparts today are the civil rights movement, the environmental movement, the women's movement, the peace movement, and so on. Brian O'Connell has argued[15] that cause organizations are the heart and soul of the independent sector, that they more than any other type of nonprofit exemplify the role that the independent sector plays in the society. If this is true, and to the extent that it is true, there is a moral dynamic in the nonprofit sector that keeps moving it toward the ethical, social, and humane aspects of our lives; and if that is true, nonprofit management is significantly more likely than for-profit or government management to encounter complex and demanding moral leadership issues emanating from organizational mission.

Let me pause here to pay homage, curiously enough, to Milton Friedman. Discussions of social responsibility are particularly vulnerable to the fashions of the moment. Clearly many of the business and public administration school ethics courses came from events like Watergate, the Vietnam War, the environmental movement, and more recently Iran/Contra, insider trading, apartheid, and a wealth of events in the Reagan administration. But reactions to events and highly visible people won't answer hard questions about ethical behavior in corporations, government, or nonprofit organizations. Those answers will only be found in careful analysis of the essential characteristics and functions of those organizations and their societal context and mandate. That is why I think Milton Friedman is at least arguing in the right way, in spite of the fact that I disagree with his conclusion, when he says that the only responsibility of the corporation is to make a profit for its stockholders.[16] What he is essentially saying is that a corporation is not that type of thing, it is not a reality to which qualities such as responsibility or morality can be meaningfully applied. He might argue that it makes as much sense to talk about the social responsibility of Mahler's Second Symphony or the Rocky Mountains as to talk about the social responsibility of a corporation. Friedman's point is actually a far more complex and substantive one than often characterized or caricatured; it is not necessary to go into it here, except to make the point that his logical approach is correct, whether or not one agrees with his factual analysis and conclusion.

It also seems clear that the characteristics of the clients served by many nonprofit organizations create special dimensions of responsibility for the managers of these organizations. The primary clients of the for-profit world are adult buyers most of whom are able to make reasonably intelligent decisions about what they buy Economic activity among non-adults, though large in absolute terms, is still a relatively minor part of the economy and is indirectly controlled to some extent by adults. The clients of government services are more mixed, since government is much more likely than business to deal extensively with children and with persons of limited faculties. When government does become involved with these more dependent populations (children and youth, the physically and mentally handicapped, etc.), clearly it has a different type of responsibility than when it deals with, e.g., taxpayers, soldiers, and speeding motorists. The nonprofit sector seems to specialize in providing services to clients who do not have strong positions the society: children, young people, women and minority groups in situations of discrimination, abused women and children, persons with limited legal or political resources, the physically and mentally ill, workers in harmful working conditions, people grieving over loved ones, immigrants, etc. This is not to say that all the clients of the nonprofit sector are in weak positions: many clients of private universities, churches, and mutual benefit organizations are anything but weak and needy. Nevertheless, it is easily observable that the nonprofit sector has a far higher percentage of "weak" clients than does either the business sector or the government sector. This clearly creates a special type of responsibility for those who manage and direct these institutions.

At this point you might be wondering, who in his or her right mind would accept a nonprofit management position, with all that responsibility? Let me close, therefore, by taking off in a seemingly opposite direction. I believe that one of the principal tasks facing nonprofit theorists and researchers is the analysis of nonprofit management and organizations from the point of view of self-interest. It has long been accepted that "money money money makes the world go around," at least in the for-profit sector. Nobel laureate James Buchanan has recently led us to think more about government officials' behavior as exemplifying the principle of self-interest first and the public interest second. If you don't find that a little disturbing, think about the possibility of viewing management behavior in the nonprofit sector as a further extension of the principle of self-interest. Yet I submit that this would not only be important and interesting research; it would also illuminate the issue of managerial responsibility, the moral aspect of leadership, in nonprofit organizations. Unhappily, some of the most truly immoral behavior in the nonprofit sector comes when the legitimate self-interest of people in the sector is ignored. Look at the working conditions in the peace movement. As anyone who has ever worked full time for a cause knows, it is exhausting as well as exhilarating, and produces burnout along with job satisfaction. Peace workers are paid pitiful salaries and usually have no medical or retirement benefits. Yet what they do is some of the most important work currently going on in the nonprofit sector. We all realize and accept the notion that few people work in the nonprofit sector to get rich, and that there is such a thing as "psychic income." But some of the cause organizations pay starvation wages, income that falls well below the official poverty line. The peace movement presents a stark example of the conflict between the morality of a cause and the legitimate self-interest of workers for that cause. We need to think more about the self-interest of managers in the nonprofit sector, and even before that we need to accept the idea that self-interest not only has a place in the sector but provides much of the energy that drives the sector. This seems at first blush to contradict our most cherished views of the altruistic nature of the sector, but after all we know enough about "altruism" both among humans and in the animal and insect kingdoms to realize that altruism and self-interest are not really opposites; they are points on a spectrum, different aspects of the same unity of individual and group behavior. Ironically, complete or extreme altruism is a very poor basis for morality, because it ignores the most fundamental needs of the organism. Or as St. Thomas Aquinas put it, "One must eat in order to philosophize." Any serious attempt to understand the nature of managerial responsibility in the nonprofit sector must consider not only what the manager owes the organization but also what the organization--and the sector, and the society--owe the manager. To go back to the etymology of "responsibility," we are talking about a pledge, a promise, a moral pact; and the pact goes both ways.

I have argued that (1) any organization and any management process involves "responsibility," the moral dimension of leadership without which any leader is insufficiently effective; (2) nonprofits, because of their somewhat unique personnel characteristics, seem to present managers with more complex responsibility than many other managers face, since nonprofits tend to be organizations "of, by, and for people," and since the people in these organizations tend to be more educated, professional, and therefore demanding of responsible and moral leadership; (3) nonprofits because of their relatively unique social, ethical, humane, and religious missions demand a certain type and level of responsibility from their managers; religious and advocacy organizations are a good example of this point, even though they are by no means the only organizations in the nonprofit sector which have such strong ethical orientations; (4) nonprofits have a significantly higher percentage of relatively "weak" clients than either business or government, with clear consequences for the nature and type of managerial responsibility involved; and (5) nonprofit managerial responsibility cannot be fully understood unless we take into account the managers' legitimate self-interest, as part of a more general inquiry into the application of the principle of self-interest to the nonprofit sector.

Generally, I have stressed that insight into the issue of management and responsibility in the nonprofit sector (or any other sector) comes primarily from analysis of the basic characteristics of the organizations and management roles involved. Morality and responsibility pertain to an organization, not to the extent that there have been recent scandals in that organization, but to the extent that the nature of the organization demands that such scandals not occur, which is after all why we made such a fuss about the scandals in the first place.

Endnotes

[1] Chester I. Barnard, *The Functions of the Executive* (Cambridge, Mass., Harvard University Press, 1938), p. 257. Or as Philip Selznick later put it: "The institutional leader . . . *is primarily an expert in the promotion and protection of values*." *Leadership in Administration*, (New York: Harper & Row, 1957), p. 28. Emphasis in the original.

[2] Barnard, p. 259.

[3] Ibid., p. 260.

[4] Ibid., p. 274.

[5] Ibid., p. 282. Thomas Watson, former chairman of IBM, made much the same point: "Consider any great organization--one that has lasted over the years--I think you will find that it owes its resiliency not to its form of organization or administrative skills, but to the power of what we call *beliefs* and the appeal these beliefs have for its people. This then is my thesis: I firmly believe that any organization, in order to survive and achieve success, must have a sound set of beliefs on which it premises all its policies and actions." *A Business and Its Beliefs* (New York: McGraw-Hill, 1963), p. 6.

[6] "Doing things the "right" way is a dominant *moral* code in the specialized work of many fine mechanics, musicians, artists, accountants, engineers, for example." Barnard, p. 266.

[7] Ibid., pp. 267-68.

[8] Ibid., p. 268.

[9] Ibid., p. 270.

[10] Ibid., p. 279.

[11] Ibid.

[12] Ibid., p. 283.

[13] Ibid., pp. 282-83.

[14] See, for example, Philip H. Mirvis and Edward J. Hackett, "Work and Work Force Characteristics in the Nonprofit Sector," *Monthly Labor Review*, 106 (April, 1983), pp. 3-12.

[15] "Values Underlying Nonprofit Endeavor," in Michael O'Neill and Dennis R. Young (eds.), *The Education of Nonprofit Managers* (New York: Praeger, in press).

[16] Milton Friedman, "The Social Responsibility of Business is to Increase Its Profits," *New York Times Magazine*, September 13, 1970, pp. 122-126.

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ACCOUNTABILITY OF THE INDEPENDENT SECTOR

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ACCOUNTABILITY OF THE INDEPENDENT SECTOR

The continued existence of the Independent Sector is dependent upon general confidence that it is serving the public. In that sense, the phrase "Independent Sector" is a misnomer. In fact the sector is accountable at all times to both the private sector and government. The result, as with many forms of regulation, is a constant tension beteween the demands of the public for assurances of proper behavior and the demands of the sector for freedom to operate to achieve its charitable[1] goals.

The purpose of this paper is to review the current methods for assuring accountability of the independent sector, to appraise their adequacy, to explore how they are likely to change and the effect of these changes on the ability of the sector to maintain its independence.

Accountability Under the Common Law

The basic method for assuring accountability of the nonprofit organizations that comprise the independent sector were devised as long ago as the sixteenth century when the common law dealing with charitable trusts was developed and a pattern for government supervision was devised to assure responsible behavior by the managers of these trusts. This law articulated a set of duties governing trustees. It also assigned the attorney general, representing the sovereign as parens patriae, the exclusive right to represent the indefinite class of individuals which these entities were designed to benefit. The concept of exclusive jurisdiction reflected the pragmatic view that no one would serve as a fiduciary of a charitable trust if he could be called to account by any member of the general public.

The nature of the duties set forth in the common law reflected the expectations of society: specifically that there should be a singular and enveloping duty to carry out the charitable purposes of the trust; that it was necessary to keep the trust property productive; and that trustees should be prohibited from diverting charitable funds by making improper investment or self-dealing. Regulatory power was ultimately lodged in

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1/ The terms "charitable" and "charities" in this paper are used in the sense they were used in the common law, encompassing the entire range of educational, scientific, religious and charitable purposes that are also described by the term "philanthropic".

the courts of equity which could remove trustees, impose surcharges and enjoin inappropriate actions.

These duties continue to form the basic law - in England and in the United States - governing the behavior of fiduciaries. Similarly, reliance on the attorney general as enforcement officer became the pattern in the United States and continues to this day in virtually all jurisdictions. Freedom was assured under this system in that, so long as the trustees acted prudently and observed any restrictions imposed by donors, neither the court nor any government official was allowed to question the methods chosen to achieve the trust's purposes.

Starting in the 19th century, the preferred legal form used to establish entities to conduct charitable activities began to shift from the charitable trust to the nonprofit non-stock corporation but, with a few exceptions, the laws designed to assure accountability of charitable trustees were applied to the directors of charitable corporations (who were and still are often called "trustees").

There were no major changes in the laws governing fiduciary duties or the methods used to assure their accountability until the middle of the twentieth century. Charities could be called to account in court by a state attorney general but, in actuality, there was little perceived need to resort to remedies of this nature. This situation changed in the mid-twentieth century with a vast expansion in the number of charitable organizations, traceable primarily to the increased importance of tax incentives for their establishment, particularly the ability of donor' to make tax deductible gifts to them.

Regulation Through Tax Laws

Both Federal and state tax laws have consistently contained exemptions for the income of charities and permitted deductions for contributions to them. The earliest of Federal statutes established the basic pattern for Federal regulation. The purposes that were described as "charitable," "educational" and "religious" were specifically to be determined under common law precedents, and the duty of loyalty to these purposes was articulated in the requirements that the organization be "operated exclusively" for its exempt purposes and that "no part of its net earnings enure" to the benefit of any individual. In addition, starting in 1943 certain charities were required to file annual information returns with the Internal Revenue Service and these reports were made available to the general public. However, until recent years the view of Congress was that accountability in the first instance was concomitant with dependence on contributions from the general public. Thus, until 1969, annual reports were required only from what we now call private foundations and then, once all organizations except churches were subject to the reporting requirement, private foundations were required to file more information than other charities. In addition, in 1950, private foundations were subjected to restraints against the accumulation of income and self-dealing. It was also in 1950 that taxes were imposed on the unrelated business income of exempt organizations in a measure designed to prevent what was perceived as unfair competition with privately owned businesses. In 1954, the percentage limit for deductions was increased for gifts to religious orders, educational institutions, hospitals, churches and conventions of churches and in 1964 it was extended to all publicly supported organizations.

The Tax Reform Act of 1969, in addition to expanding reporting requirements, contained more pervasive federal regulation than anything previously enacted. The new private foundation rules, imposing excise taxes not only on the charity but also on its managers, reflected a recognition that the enforcement tools available in state courts of equity were more effective for assuring compliance than loss of exemption. Under these rules it was also possible to preserve charitable funds for the continued benefit of the general public. However, federal tax rules are of necessity designed to protect the integrity of the tax system. Accordingly, prohibitions against accumulation and rules limiting the holding of interests in business entities reflected the desire to obtain immediate benefit for society in exchange for the tax benefit given to the entity and its contributors, a concept with no counterpart in fiduciary law.

State Regulation of Charities Since 1950

Since 1950, twelve states have enacted legislation requiring certain charitable trusts and corporations to register and file reports with the attorney general. The purpose of this legislation was to assure that the attorney general would have sufficient information to permit him to enforce proper administration of charities. In addition, although Congress continued to believe that reliance on contributions from the general public would assure accountability of publicly supported charities, the enforcement authorities in some states became concerned with the high cost of fundraising and instances of deceptive solicitations. The result was legislation requiring, in most instances, registration with a state authority; the filing of annual returns; and a requirement that solicitors be licensed and bonded. Some of these statutes placed limits on the amounts that could be spent on fundraising. However, the United States Supreme Court in cases decided in 1980 and 1984 held that state regulation of this sort violated constitutional rights of free speech and equal protection. Another method for regulating solicitation embodied in several of these statutes is to require disclosure at the time of solicitation of the cost of fundraising, expressed as a percent of total funds raised. The constitutionality of provisions of this nature contained in the laws of Maine and North Carolina is to be decided in 1988 by the United States Supreme Court.

Research Papers sponsored by the Commission on Private Philanthropy and Public Needs (The Filer Commission) contain studies summarizing the status of Federal and State regulation in the early 1970's and an analysis of the effectiveness of fundraising percent limits. They also include important discussions of the need for uniform accounting standards and the benefits and limits of self-regulation. Overall, they emphasize the lack of information on the extent of abuse and the effectiveness of existing remedies.

In those states with active enforcement programs, the offices of the attorney general have been able to correct a number of abuses involving self-dealing and improper diversion of funds. Of equal importance, they were instrumental in assuring that provisions governing charities with obsolete purposes or impracticable provisions were revised by the courts to make them more responsive to current needs. However, as the size and nature of charitable activities expanded, tensions relating to the appropriate nature of charitable enterprise emerged. The restructuring of hospitals into several component entities, following the pattern of parent and subsidiary corporations found in the business world, was a pervasive development, but there were also a number of attempts by the trustees of exempt organizations such as HMO's to convert them into private corporations, an attempt that was blocked in states with active enforcement programs but that was apparently successful elsewhere. The response in the states to these developments was confused. For example, the duty of loyalty of trustees of subsidiary corporations to their parent was unclear. In addition, it has proved difficult to obtain adequate information regarding the operation of for profit subsidiaries. The result has been to create an atmosphere of distrust. For example, the Massachusetts Attorney General attempted unsuccessfully to block efforts by a charitable corporation to sell its hospital facility to a for-profit corporation, even though it planned to treat the proceeds as endowment and to act as trustee of a grant-making health care foundation. The Attorney General did succeed in another case in preventing the sale of another medical facility and use of the proceeds for the benefit of its parent. In neither case was there precedent for approving or disapproving the proposed action and the resulting uncertainty has had a negative effect on relations between the Attorney General and the charitable community.

Recent Developments in Accountability
1987 - The State Scene

Developments in the year 1987 give us some insight as to where we are and where we might be in the year 2000. The enforcement tools have not changed. State programs to supervise the general activities of charitable organizations have not expanded. In fact, there has been some contraction in the scope of the programs in Ohio and California. However, state officials have established better communications among themselves and with the Internal Revenue Service and have unified reporting requirements, principally by using Forms 990 and 990 PF as the basic vehicle for obtaining information.

The major expansion of regulation at the state level has been in connection with the regulation of solicitation. There are now 36 states with reporting statutes, ten of these enacted or substantially revised since 1986. Much of the impetus for this recent expansion came with the adoption in 1987 by the National Association of Attorneys General of a Model Act to Regulate Solicitation. The Act is not free of controversy. The higher education community has mounted efforts to be exempted from its provisions and it contains restrictions on paid solicitors which raise the constitutional issues of equal protection and free speech now before the Supreme Court. Nonetheless, it appears likely that the Model Act will be adopted in an increasing number of jurisdictions.

An important recent development at the state level has been a widespread reappraisal of the basis for the exemption from state and local property and income taxes granted to charities. The initial focus was on alleged business activities of certain athletic clubs, but it was soon expanded to encompass other charitable organizations previously considered inviolate such as hospitals and health related entities. Some of the impetus for this reappraisal was traceable to the activities of the Small Business Administration which, starting in 1980, mounted an effort to halt what it conceived as harmful advances of the non-profit sector into commercial pursuits. This effort has included organizing businessmen to sponsor local and state initiatives to remove tax exemption for charities engaged in "commercial activities".

Another development in the states in 1987 ironically was directed toward alleviating the liability of charitable fiduciaries rather than increasing their duties. In a direct response to widespread and growing fears that charitable fiduciaries would be subject to personal liability for failure to adequately monitor the activities of agents, coupled with a drastic increase in the cost of liability insurance, bills were introduced in the legislatures of almost every state granting immunity in suits seeking monetary damages for negligence and, in some cases, for gross negligence, or expanding the scope of existing immunity statutes.

1987 - The Federal Scene

In the chronology of the Federal government's relations with tax exempt organizations, 1987 will undoubtedly be associated with the name of Congressman Pickle, D-Tex. just as the names Walsh, Reece, Cox and Patman are associated with earlier congressional investigations of exempt organizations, and, particularly in those earlier investigations, private foundations. Congressman Pickle, as Chairman of the Ways and Means Oversight Subcommittee, held three sets of hearings on the activities of exempt organizations during the spring and fall of 1987. The first, held in March, dealt with political and lobbying activities. The Committee heard testimony indicating that funds obtained from sales of arms to Iran were funneled through exempt organizations and used to oppose candidates for political office in contravention of Code provisions. At the conclusion of the Hearings, the Oversight Subcommittee issued 13 legislative recommendations. These ultimately became part of the Ways and Means Committee's Revenue Reconciliation Bill of 1987, which, with certain amendments adopted during Conference, became part of the Revenue Act of 1987 that was enacted on December 22, 1987.

The new provisions are noteworthy because of the patterns of regulation they contain. They have expanded accountability by requiring that all exempt organizations, not just private foundations, make Forms 990 and 1023 available for public inspection at the organizations' offices. They impose excise taxes on organizations and their managers, in the manner previously applicable only to private foundations, to publicly supported charities which engage in certain prohibited political or lobbying activities. They impose point of solicitation disclosure requirements on certain tax exempt organizations, again with excise taxes on the organization and its managers as the penalty for non-compliance. Finally, they provide the Internal Revenue Service with broad new powers to obtain information regarding transactions with affiliated entities and assess taxes and seek injunctions to prevent "flagrant abuses" of the prohibition against making political expenditures.

The second set of hearings which was held in May focused on competition with the private sector and the unrelated business activities of exempt organizations. Testimony by government officials and members of the private sector evidenced a dramatic change in public attitude toward exempt organizations and pressaged not only changes in the regulatory pattern, but a reappraisal of the rationale for exemption. This was in part a reaction to changes in the scope and nature of exempt organization activities already described, but was spurred in large part by the Small Business Administration's campaign. A uniform theme in all of the testimony was the lack of information on the exact scope of business activities - whether related or not. The Commissioner of Internal Revenue, Lawrence B. Gibbs, in his testimony before the Subcommittee, expressed his belief that "unfair competition" would be an unworkable standard for monitoring business activities, and indicated his belief that, with the expanded audit activities already in place, the Service could meet the call for better regulation .

In the Treasury Department's testimony, 17 major issues relating to business activities of exempt organizations were identified as needing review. No specific legislative recommendations were made, but the detailed discussion of problem areas indicated a likely basis for future legislative changes. None in themselves would depart from the existing regulatory pattern. However, Assistant Treasury Secretary O. Donaldson Chapoton provided a new rationale for tax exemption that was noteworthy. After remarking that the services provided by exempt organizations are similar to those provided by government and that limits on the scope of exemptions are appropriate and necessary, he stated:

> This nation has prospered through its reliance on a private, market-based economy to supply necessary goods and services. The role of government generally has been restricted to those socially important activities not adequately supported by the private sector. The role of the quasi-governmental, not-for-profit sector should similarly be restricted to that of supplementing, and not supplanting, the activities of for-profit businesses. Thus, tax exemption for public charities should be restricted to those areas where the quality or quantity of goods and services that would be produced strictly through market forces is inadequate. (emphasis supplied)

This view draws from and complements the position of several economists and political scientists who who base their position, however, on the issues of efficiency and the proper role of the tax system, rather than the needs of the private sector. Their view was exemplified in testimony presented to the Oversight Subcommittee on June 30, 1987, by Professor Henry Hansmann of Yale Law School who argued that exemptions should be granted only to organizations substantially dependent on contributions from the general public or, in the case of those which rely primarily on fees for services (such as hospitals, day care agencies, HMO's and fitness centers), only if there is insufficient competition from the private sector to asure that the services will not be provided by for-profit organization at a lower price.

The third set of hearings conducted in 1987 by the House Oversight Subcommittee dealt with the financial dealings of what it described as television ministries. Under existing law, religious organizations need not seek an advance determination of tax exempt status. In addition, they are exempted from annual filing requirement, and protected from IRS audit unless the Service has met certain specific standards. During the hearings the Commissioner and his aides pointed to the severe limits on the Service's ability to monitor churches, particularly the lack of any requirement to seek an initial determination of tax exempt status. Testimony was presented suggesting that certain religious organizations should be subjected to expanded reporting requirements. Several church representatives indicated agreement, but others raised constitutional objections. The general sense of the hearings was that a number of Congressmen would be willing to reconsider the propriety of the current broad exemption of religious organizations from the regulatory process.

In November of 1986, the Treasury Department released Proposed Regulations under Section 501(h), enacted 10 years previously, which permits certain tax exempt charities to elect to be subject to dollar limits on the amounts they may properly spend for lobbying. The Proposed Regulations were sufficiently restrictive to arouse widespread concern and to cause several Congressmen to call for their withdrawal. In response, the Commissioner of Internal Revenue agreed to postpone final promulgation and arranged for further study. He then appointed an Advisory Group on Exempt Organizations comprised of 18 individuals who met in October of 1987 and February of 1988 to discuss the lobbying provisions as well as the other current issues affecting exempt organizations. The willingness of the Service to work openly with representatives of the independent sector on issues of common concern was a new development offering hope of improved regulation in the future.

A final 1987 development at the federal level to be noted was a proposal to impose a five percent excise tax on the investment income of tax exempt organizations. This was one of several revenue raising options proposed by the staffs of the House Ways and Means Committee and the Joint Committee on Taxation. Protests from all segments of the independent sector were immediate and the provision was not among the final options considered by the tax writing committees. Nonetheless, one of the Treasury Department recommendations to the Oversight Subcommittee at its Hearings on Competition was to remove the tax exemption for passive income of social welfare organizations, trade associations and labor unions, increasing the likelihood of taxes being imposed on this source of income in the future.

Issues for the Future

Each of these developments presages changes in the regulation of charities at both state and federal levels; some immediate, others long-term. Reliance on the tax laws as the primary source of regulation is not likely to change. What we are seeing, however, are attempts to refine regulatory tools. This is likely to continue. One can quite easily predict further expansion of the regulatory scheme embodied in the private foundation rules to publicly supported charities - especially as applied to self-dealing and taxable expenditures, encompassing as they do excessive compensation and other forms of private benefit which have previously been subsumed in the concept of private inurement. It is also likely that many, if not all, of the specific suggestions relating to the unrelated business income tax identified by the Treasury as warranting additional study will be enacted as early as 1988 or 1989. Cooperation between the Internal Revenue Service and the independent sector is greater than it has ever been. This is likely to ensure that new rules will be enforced with greater understanding of their purpose and appropriate application by the regulators.

However, improved enforcement tools and their more rational application of them will not stop the ongoing reassessment of the basis for exemption. If the result is to remove exemption from all but those charities which rely primarily on contributions or which do not conduct "commercial" activities, two further major changes are likely to occur. First, the federal government will concern itself with the regulation of solicitation and, for those charities relieved from federal regulation by virtue of being subject to tax, state regulators will likely attempt to fill the gap by enforcing the common law fiduciary rules. Thus, the basic question of who is to regulate - the federal government or the states - may be answered in new ways. In regard to solicitation, proposals have been made from time to time since the 1970's to require point of solicitation disclosure of fundraising costs as a condition of continued tax exemption or use of the mails. Should the Supreme Court hold similar state requirements unconstitutional, the proponents of these measures may well look to the Congress to accomplish what they cannot do under state law.

The second long-term development will come as a result of broader recognition that the Internal Revenue Service is not the most appropriate agency to regulate the independent sector. It lacks the more refined tools available to state equity courts to compel compliance. It is not well placed to police disclosure provisions. Even if granted equity-type powers, its staff is neither by training nor inclination suited to enforcement that is not designed to raise revenue. Just as the ERISA rules are enforced in part by the Service and in part by the Labor Department, so too charities may find themselves subject to the jurisdiction of another agency. The Federal Trade Commission and the Post Office have already been suggested as appropriate agencies to police solicitations and the FCC might regulate television ministries. Alternatively, Congress may decide that a separate enforcement agency should be established. The issue of federal preemption of state law would then require reexamination. Some of these regulatory possibilities were raised and discussed in various of the Filer Commission papers. They warrant another look.

This, then is the start of a research agenda for the future. It should also include a fresh look at the effectiveness and propriety of regulatory measures to deal with public solicitations. No studies have been conducted to determine whether point of solicitation disclosure of fundraising costs actually effects giving patterns. Programs to improve public understanding of the "costs" of fundraising are just now underway. We need to know if these programs will lead to better informed contributors. We should also consider whether there is sufficient evidence of abuse to warrant expanded regulation designed to protect contributors - weighing the increased costs to government and to the charities against the benefits sought to be obtained, particularly if the regulatory pattern will involve 50 different laws in 50 different states.

The greatest need for information, however, relates to the "business activities" of exempt organizations. This need was the one common thread in the testimony presented at the 1987 Hearings on Competition. Lack of knowledge of the scope of non-profit and for profit activities of exempt organizations undoubtedly contributed to the misunderstandings expressed by some

Congressmen, who seemed to believe that the conduct of unrelated activities that were subject to tax was per se improper. In fact, the enforcement problem appears to be not with the filers, but with those who do not understand or who ignore the rules. The larger problem, however, is the extent to which exempt organizations have established for-profit companies and whether, in so doing, have diverted funds or attention, or both, from their original mission to the detriment of the sector. In terms of the standards by which we measure accountability, this is the major unresolved issue. The tension is between, on the one hand, those who believe that the business of charity is charity, not business, and that the adoption of business techniques and standards deter managers from the true goals of the sector and, on the other hand, those who believe that charities will not survive unless they apply some of the techniques and standards of the business sector to their activities. This is undoubtedly as much a philosophic as an economic or legal issue. In terms of the study of accountability, it needs to be addressed from each of these aspects. It is likely that a middle ground will emerge. We will demand use of private sector techniques to assure efficiency, while retaining the overarching dedication to public benefit which is the essence of philanthropy as the ultimate standard for accountability. New standards will, in turn, require new enforcement tools. In devising them, we must assure that the need for them has been demonstrated; that the costs they impose in terms of limiting independence are outweighed by that need; and that they represent the least obtrusive measures that can be devised. This ultimately is the challenge that accountability has always posed for the independent sector and that it will continue to pose in the years 2000 and after.

SECTION FOUR:

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ADVOCACY MOVEMENTS FOR CHILDREN SINCE 1960

by

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Prepared for the 1988 Spring Research Forum
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Public Policy and Philanthropy"

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In a paper presented at the 1985 Spring Research Forum I discussed the ways scholars have dealt with, or avoided dealing with, advocacy in histories of English and American philanthropy, the growth of advocacy and empowerment movements in the United States in recent decades, and the legislative history of the Public Charities Lobbying Act of 1976. The present paper first comments on the relation between service and advocacy in modern philanthropy, and then focuses on some of the agents, problems, and prospects of advocacy for children.

Service and/or Advocacy

The strong opposition expressed by the philanthropic community to the regulations proposed by the Internal Revenue Service in November 1986 to implement the Public Charities Lobbying Act demonstrated the importance charitable organizations of all kinds and diverse points of view attach to advocacy, and their resistance to governmental attempts to curtail lobbying and other efforts to influence public policy by nonprofit groups. Independent Sector, whose roots go back to the Coalition of Concerned Charities which worked for passage of the 1976 law, has taken a leading part in securing revision of the regulations, and also in opposing efforts by the Reagan administration to exclude advocacy organizations from the Combined Federal Campaign.

"By devoting its resources to a particular activity, a charity expresses a view about the manner in which charitable goals can best be achieved." The quotation is from a dissenting opinion by Justice Blackmun in a Supreme Court case involving the constitutionality of Executive Order No. 12404 (February 10, 1984) excluding charities seeking to influence the determination of public policy from the Combined Federal Campaign. Blackmun argued "Charities working toward the same broad goal, such as 'improved health' may have a variety of views about the path to the goal." Service charities, for example, believe the best approach to "improved health care" is through medical research, public education, detection programs, or direct care of the sick. Advocacy organizations, on the other hand, believe the best way to achieve the goal is "by changing social policy, creating new rights for various groups in society, or enforcing existing rights through litigation, lobbying, and political action." Blackmun characterized the Administration's distinction between service and advocacy charities as "blatantly view-point oriented" and urged that the Executive Order be struck down.[1]

The difference between service and advocacy charities is seldom absolute. Health and welfare organizations may elect, as a general rule, to follow either the service or advocacy path, but, from time to time circumstances may make it necessary or advisable for them to take the other path. Two of America's most famous voluntary agencies, the New York Association for the Improvement of the Condition of the Poor and the Charity Organization Society of New York, pioneered not only in the development of casework services but also in campaigns for public health, better housing, and welfare reform; their successor, the Community Service Society of New York, decided in 1971 to end individual and family caseworker services in order to concentrate its resources on community services and social reform. Service and advocacy are difficult to separate when a charity offers help to the needy in such a way as to demonstrate its need and feasibility and to rebuke public indifference to the people served.[2] The doctrine that prevention is cheaper and better than cure is so widely accepted in principle, if not always observed in practice, that nearly all health and welfare organizations feel an obligation to advocate preventative action ("building a fence at the top of the cliff") instead of resting content with the thankless tasks of picking up the pieces and clearing the wreckage. Voluntary effort on behalf of a group such as homeless families seems to lead inevitability from provision of temporary shelters to attempts to compel city, state, and national governments to take more vigorous action.

"Are voluntary agencies needed, in view of the great expansion of governmental health and welfare activities?" The question, raised in 1961, was to come up repeatedly in the Kennedy-Johnson years as federal programs encroached further on the traditional realms of philanthropy, and the "lopsided availability of tax dollars over voluntary dollars" for welfare, education, and health become ever more apparent.[3] Before the decade of the 1960s closed, however, both service and advocacy organizations had proved their usefulness, in different ways, in the American version of a welfare state. In each case the roles assigned to or assumed by voluntary agencies stemmed from fear and distrust of bureaucracy and big goverment. Not civil servants but employees of voluntary agencies working under grants from or contracts with government, delivered the services made available in new fields and to a broader clientele by new federally-funded social programs. Even before the social programs were enacted other tax-exempt organizations, whose right to engage in legislative lobbying was (until 1976) severely limited by the tax code, began to monitor the enforcement of executive orders, existing laws, and court decisions by public officials. The Southern Regional Council, a foundation-supported equal-opportunity organization, led the movement to secure more stringent enforcement of civil rights, desegregation, and anti-discrimination laws, and, in cooperation with other advocacy groups, investigated and reported on the misuse by school districts of funds made available by the federal government for compensatory education of poor children. This study, which led the Department of Health, Education and Welfare to seek to recapture misused funds and to institute and enforce stricter guidelines and standards inspired coalitions of advocacy groups to monitor federal performance in housing, employment, civil-rights enforcement, and many other areas.[4]

"Riding herd on government programs," as Harold C. Fleming, former director of the Southern Regional Council, called the monitoring process, was a familiar tactic of some advocacy organization and, of course, was regularly practiced by business, labor, farm, and professional associations. During and after the 1960's monitoring became much more common as welfare recipients, consumers, the physically handicapped, developmentally disabled, and the elderly became conscious of their rights and militant in their demands for observance of them. What they wanted, in most cases, was to have the service authorized by statute provided adequately and appropriately. In 1967 a coalition of women's organizations sponsored a study of the extent to which the school lunch program established in 1946 was meeting, or failing to meet, the needs of poor children. The study, Their Daily Bread, revealed shocking inadequacies in the coverage, financing, and administration of the program: of 50 million school children, only 18 million participated in the school lunch program, and fewer than 2 million were able to get free or reduced-price lunches; the poorer the school district the less likely its children were to be served.[5] The findings of Their Daily Bread were given further publicity in Hunger, U.S.A., the report of a citizens' inquiry group which led to the formation of the Senate Select Committee on Nutrition and Human Needs.[6] For almost a decade after 1968 the Select Committee held hearings, assembled expert testimony, and worked to improve the coverage of the nation's child nutrition programs.

Since the 1960s public interest advocates, drawing on the example and experience of organizations like the NAACP Legal Defense and Education Fund and the American Civil Liberties Union, have made wide use of litigation as a means of changing public policy. Like monitoring, this is an instance of the use in the public interest of methods long employed by private interests to modify or overturn social legislation or other measures they oppose. In a recent examination of test case litigation for children Robert M. Mnookin sketches a brief history of the rise of public interest law firms:

> The Legal Defense Fund foreshadowed the public interest law movement. During the late 1960s and throughout the 1970s, with support from charitable foundations and the federal government, new organizations not dependent on fees from clients were established to use law to promote change on behalf of groups and interests said to be previously unrepresented. Some public interest law firms handled many types of cases. Others specialized in areas such as the environment, mental health law, welfare rights, civil rights, consumer protection, or the particular concerns of racial and ethnic minorities. During the same period, the federal government established and subsidized a legal services program to better meet the legal needs of the poor. In addition to serving the needs of individual

clients, legal service lawyers, especially those employed in specialized back-up centers, used test-case litigation to change policies. These new institutions, bringing together reform-minded lawyers, have played an important role in expanding the policy-making activity of courts.[7]

As defined by the Council of Public Interest Law a public interest law center is "a non-profit, tax-exempt group that devotes a large share of its program to providing legal representation to otherwise unrepresented interests in court or administrative proceedings involving important questions of public policy." A survey conducted by The Council in 1979-80 found 117 centers, each with at least one attorney on its staff and altogether employing more than 700 lawyers. The federal government and foundations, each contributing about the same share, provided the largest part of the centers' total income of $53 million. Despite the bitter opposition of the Reagan administration to both voluntary and federal legal service programs a 1984 directory listed 125 public interest law centers. Some of them described their major program emphasis as "Business Oriented/Free Enterprise."[8]

Both the expansion of judicial power that has taken place in the last thirty years and the often controversial activities of public interest lawyers are currently under attack by political and academic critics. From the standpoint of philanthropy, public interest law is interesting and important because it combines and demonstrates the compatibility of service (legal representation) to clients with advocacy of causes.

Advocacy for Children

On Christmas Day 1987 *The New York Times* reported the revival of charity in Russia where, in the preceding six months, a dozen groups sought donations for various causes. At least two organizations proposed to aid the disabled, but differed on whether "political education" (advocacy?) or "practical help" (service?) was what was most needed. Another group took as its clientele 300,000 orphans in state-run nurseries, schools, and understaffed and poorly equipped vocational schools. "Children belong to no one," explained the organizer of the children's fund. "Children are our future and everybody should help them."[9]

Americans who read the future in the circumstances of today's children worry about the vast numbers of children under six years of age who belong to families living in poverty (20 to 25 percent of the total number, 40 percent of Hispanics, more than 50 percent of Blacks); about 3 million children in homeless families, about an undetermined number, estimated at several hundred thousand "orphans of the living" in foster homes; and are concerned that a high percentage of babies expected to be born in the next decade will have mothers who are unwed teenagers.

These and other circumstances will make it more difficult for families to meet their children's needs without assistance from others; they increase the need for advocacy to protect and promote the children's interests but do not necessarily make the advocates' tasks easier, or intrusion or intervention in families more welcome.

Friendly critics fault child advocates for substituting talk for action, inability to agree on goals, attending to the needs of some groups of children while ignoring those of others, and favoring indirect solutions such as aid to families rather than programs having a direct impact on children.10 A less friendly critic, Robert H. Mnookin, points out a "troubling paradox":

> children need advocates because in most circumstances, young persons cannot speak for and defend their own interests. And yet, because children often cannot define their own interests, how can the advocate know for certain what those interests are? More fundamentally, how can there be any assurance that the advocate is responsive to the children's interests, and is not simply pressing for the advocate's own vision of those interests, unconstrained by clients?

Moreover, except in unusual cases (Mnookin argues), "value and prediction problems make the best interest of children indeterminate for legislators, administrators, and judges alike."11

Mnookin's objections can be raised against advocacy for animals, the environment, historic preservation, endangered species, the mentally ill and incompetent, and against advocacy advertising by business, and spokesman for or against public policy in many areas of social and economic concern. Legislators, administrators, and judges find it hard to agree on what is in the best interest of the nation, the human race, and, in most cases, adults. Advocates for children have not spoken with one voice nor monopolized the floor in debates on children's issues. the victories they have won have been achieved after consideration of alternate proposals and are products of what Justice Holmes called "free trade in ideas."12

In this century child advocacy organizations have worked through state legislatures and Congress for child labor, juvenile court, and compulsory education laws, for the establishment of the United States Children's Bureau, for promotion and protection of child and maternal health, for programs to aid dependent children in their own homes, for expansion and improvement of child welfare services by public and voluntary agencies, for equal educational opportunities for minority children, and for extending health care and education to handicapped children. Since 1960 other advocates, often suspicious of the paternalistic, protective approach of traditional "welfare" advocates, have gone to the federal courts to seek recognition for some of the rights adult citizens enjoy under the Bill of Rights and due process and other clauses of the Constitution.13

The United States Children's Bureau differed from voluntary child advocacy organizations not only in that it was a government agency but in its broad mission "to investigate and report... upon all matters pertaining to the welfare of children and child life among all classes of our people." In the 1960s, a half century after its founding (1912), the Children's Bureau's interest in all children, rather than just in those currently deemed at risk, and its concern for the "whole child," physical, mental, and social, seemed old-fashioned to administrators accustomed to dealing with specific issues in "problem-solving" ways. An Executive Order issued in 1969 early in the Nixon administration dismantled the Bureau and consigned it to an inconspicuous place in the federal hierchary. Except on ceremonial occasions little has been heard from the Bureau since then.[14]

In 1987 Otis R. Bower, M.D., Secretary of the Department of Health and Human Services, used the occasion of the seventy-fifth anniversary of the founding of the Children's Bureau to disclaim "a federal monopoly on child-caring and protection." Instead he saluted the achievements of "grassroots individuals and organizations, professional groups, foundations, and voluntary, private and public child welfare agencies." Thirteen persons, including Vincent De Francis former director of the Children's Division, American Humane Association, David Fanshel of Columbia University, and Joseph H. Reid, former executive director of the Child Welfare League of America, received awards in recognition of their contributions to the well-being of American children. Most of the honorees had been active in the movements for the prevention and treatment of child abuse and improvements in child welfare services, especially adoption and foster care.[15]

Child abuse was rediscovered as a social problem in the early 1960s following a decade of research in pediatric radiology which led physicians, more or less against their wills, to conclude that some children had been assaulted by parents or guardians. The extent of the problem and the shortcomings of existing service for the victims were brought to the attention of the Children's Bureau by Vincent De Francis, formerly with The New York Society for the Prevention of Cruelty to Children, who in 1955 became director of the Children's Division of the American Humane Association. Interest in child abuse increased both among social workers and pediatricians, and following publication of "The Battered Child Syndrome" in the Journal of the American Medical Association in 1962, popular magazines ran numerous articles on child abuse. In 1963 the Children's Bureau circulated a model state law encouraging the reporting of physical abuse to physicians; the American Academy of Pediatricians and the Council of State Legislatures proposed other versions. Before the end of the 1960s all states had adopted legislation encouraing or requiring physicians, teachers, and others involved in child care to report suspected cases of child abuse to public authorities.[16]

In 1974, one hundred years after the founding of the New York SPCC, presented with a bill supported by veto-proof majorities in both houses of Congress, President Nixon signed The Child Abuse Prevention and Treatment Act into law. The measure, whose principle sponsor was Senator Walter F. Mondale, authorized funds for research and demonstration projects and for discretionary social service grants to the states. It was intended, not to eliminate child abuse, but to ameliorate the problem by identifying and assisting programs that seemed worthy of further study and replication.[17]

The limited scope of the law, probably all that was attainable at the time of its enactment, has been criticized for treating child abuse as a form of deviance, correctable by therapeutic measures, and for emphasizing its psychological origins, rather than attacking its roots in social and economic injustice.[18] On the other hand, state reporting laws and court decisions dealing with child abuse and neglect have come under attack by advocates of family privacy and autonomy.[19] The pendulum of public opinion swings back and forth between concern for battered children and resentment at government intrusion in family matters as newspaper report and communities react to instances of children murdered or severely injured by parents and other cases of seemingly unwarranted public intervention in private relations between parents and children.[20]

Goodwill and moral outrage are not sufficient to solve the complex problems presented by the 200,000 or more child abuse (now often called maltreatment) and neglect cases coming before American courts-- family, juvenile, probate, and general jurisdiction -- each year. Since 1979, when the National Legal Resource Center for Child Advocacy and Protection (NLRCCAP) of the American Bar Association began work with two attorneys, it has attempted to help the courts improve their procedures in these cases so as to arrive at more equitable and responsibile decisions. The Center, whose director, Howard A. Davidson, was among those honored at the Children's Bureau 75th Anniversary, has published a manual for judges in maltreatment and neglect litigation as well as publications for bar associations, individual attorneys, and social workers. Much of its work in the field has been supported by the National Center on Child Abuse and Neglect, an agency created by the 1974 Child Abuse Prevention and Treatment Act.[21]

In 1978, when Congress renewed and widened the scope of the 1974 law it added a second title, "Adoption Assistance," which laid the groundwork for anticipated reforms in foster care. Rep. George Miller of California, who in 1977 brought the "crisis in foster care" to the attention of Congress, declared that a system intended to provide short-term shelter for children during periods of emergency had become "a system of indeterminate long-term placements" in which little effort was made either to restore the child's own family or find a suitable adoptive home. No one defended the defects Miller cited or questioned their seriousness, but advocates of foster-care reform, including the Child Welfare League of America and the Children's Defense Fund, differed on the changes necessary, and officials of the Carter administration and members of Congress found it difficult to reach agreement on corrective action. In 1980, however, Congress passed and President Carter signed a comprehensive measure providing for encouragement of adoptions of hard-to-place children and mandating reforms in foster-care practices and funding.[22] The Adoption Assistance and Child Welfare Act has been hailed as "the most important piece of child welfare legislation enacted in the past twenty years, a blueprint for a new combined effort on the part of the judicial, executive, and legislative branches to preserve families, and if necessary, to build new ones."[23] To date, however, the statute remains, for the most part, only a blueprint because during the Reagan administration neither the federal government nor states has made a vigorous effort to enforce its mandates or fund the family counseling and mental health services intended to reduce the need for foster care.[24]

Two organizations whose contributions to children were not recognized at the Children's Bureau anniversary celebration were the National Child Labor Committee and the Children's Defense Fund. The former, one of the nation's oldest extant child advocacy groups (founded in 1904) continues to act as a watchdog over child labor legislation but, since 1946, has given increasing attention to helping young people gain employment and work experience. In 1980, for example, NCLC completed a compendium of child labor laws in all fifty states, the first of its kind, produced a series of guidebooks for supervisors of youth work programs, and helped found the National Youth Employment Coalition. It currently promotes improvement in cooperative education programs in high schools and employment and training programs for teenage parents. NCLC, which has long taken an interest in the children of migrant farm workers, helped draft the Migrant Education Act of 1967, and has monitored its administration.[25]

The Children's Defense Fund, organization 1973 with Marian Wright Edelman as president, grew out of the Washington Research Project, an organization of public interest lawyers, researchers, and public policy monitors. In the Fund's early years it took an adversarial stance against big government, using research and litigation to show families their rights in dealing with bureaucracy and to point out flaws and inequities in federal-state welfare and education programs. In publications such as Children Out of School in America (1974), Children in Adult Jails (1976), Children Without Homes (1978), and Children Without Health Care (1981) CDF showed the gulf between promise and reality in public provision for poor, minority, and handicapped children. Despite its name CDF, like its founder, has been more of a family advocate than a doctrinaire supporter of children's rights. Children Without Homes, for example, emphasized the need for services to help troubled families in order to keep as many children as possible out of foster care, and restore them to their own homes as quickly as possible.

After the Reagan administration's first round of reductions in appropriations for children's programs CDF emerged as a vigorous and effective lobbyist against further cuts. Through a monthly newsletter and an annual Children's Defense Budget it has rallied support for the programs and has kept readers advised of the effect of public policy on families and children. CDF's analysis of the impact of the Fiscal Year 1988 budget on children characteristically deals with the extent of poverty among children "and the increasing inadequacy of basic wages to meet many families' direst needs."[26]

CDF has branches in five states: Mississippi, Ohio, Texas, Virginia, and Minnesota. In 1986 the agency launched a five-year media campaign directed directly to teenagers on the risks of teen pregnancy.

In the span of this paper I have been able to deal with only a few of many important advocacy organizations for children. Every day the need for advocacy directed toward improving benefits and services for children at both the federal and state levels is brought home by accounts of children growing up in poverty, homeless, and with little reason to face the future with hope. Continuing advocacy for children on a broad front ranging from daycare, foster care, education, health housing, and welfare is essential to counteract "advocacy advertising" presenting the arguments of business corporations against government regulation and intervention and the ostensibly scholarly and authoritative publications of research centers promoting laissez-faire social policy.

Not all the news is bad. Medicaid, the largest federal program for the poor, has expanded during the Reagan years. The Annie E. Casey Foundation, one of the twenty wealthiest in the country plans to focus its programs and resources on efforts to help children at risk. Scholars report new activism and liberalism at the state level, and some communities have developed innovative services to help mothers and babies in the same centers. In January 1988 Governor Mario Cuomo presented the New York State legislature with a plan for increased health and education programs for children. The Committee for Economic Development, in a hard-hitting report, Children in Need, has pointed out urgent economic reasons for directing more of the nation's resources to meeting the needs of disadvantaged children. CED asserts:

> The nation cannot continue to compete and prosper in the global arena when more than one-fifth of our children live in poverty and a third grow up in ignorance... The nation can ill afford such an egregious waste of human resources... Allowing this to continue will not only impoverish these children, it will impoverish our nation - culturally, politically and economically.[27]

The recommendations of CED in Children in Need (investment of more public funds in quality child care and pre-school education for disadvantaged children and pre-natal care and parental instruction for teenagers), as well as evidence from other sources suggests that day care and education at all levels will be major areas of activity for child advocates in the near future. Improvements in foster care, including monitoring the administration and enforcement of the Adoption Assistance and Child Welfare Act of 1980 will continue to hold high priority. Hearings conducted by Congressional Committees such as the House Select Committee on Children, Youth, and Families chaired by Rep. George Miller highlight children's problems and what is being done to meet them in various sections of the country. Child advocates can find wide opportunities for action at the state and local levels. "Although all levels of government must strengthen their commitment to assisting children in need," declares CED," federal leadership on this issue is crucial at this time to guide reform efforts and to inspire participation from the varied segments of our national community."[28] One way advocates can help correct the "vacuum of leadership" at the federal level is to work for the restoration of the United States Children's Bureau to its former place of importance and influence in the national government and the counsels of the nation.

Notes

1. Blackmun, 1985, p. 20.

2. See, for example, Sturz, 1987.

3. Hamlin, 1961, p. 4; see also Levin, 1964, p. 163 and 1971, II, 15, 19.

4. Fleming, 1972; on lobbying by advocacy organizations before 1976 see Caplin and Timbie, 1975.

5. Committee on School Lunch Participation, Their Daily Bread, 1967. Jean Fairfax was chairman of the Committee on School Lunch Participation; the sponsoring organizations were Church Women United, National Board of the Y.W.C.A., National Council of Catholic Women, National Council of Jewish Women, and National Council of Negro Women; Florence Robin was Directory of the study.

6. Citizens' Board of Inquiry Into Hunger and Malnutrition in the United States, 1968; on the Citizens' Board see Kotz, 1969 and Mayer, 1972.

7. Mnookin, 1985, pp. 7-8.

8. Clovis and Aaron, 1980, p. 6; Alliance for Justice, 1984, pp. 13-17.

9. Barringer, 1987.

10. Sponseller and Fink, 1982, pp. 14-15.

11. Mnookin, 1985, pp. 24, 43. Mnookin's comments were directed mainly, but not entirely, at the activities of public interest lawyers in child advocacy cases. For additional comments in legal advocacy for children and youth see Davidson and Horowitz, 1986.

12. Abrams, v. U.S. 250 U.S. 616 (1919) at p. 630.

13. Steinfels, 1982. p 237; see also Mnookin, 1985, pp. 55-57.

14. Bremner, 1983a.

15. Reece, 1987.

16. Nelson, 1984 pp 2-3, 11-13, 39-44; Steinfels, 1982, p. 229. On the American Humane Association and New York Society for Prevention of Cruelty to Children, see Romanofsky, 1978, I, 83-87; and II, 628-635.

17. Bremner, 1983b, p. 95.

18. Ibid., and Nelson, 1984, p. 3.

19. Steinfels, 1982, p. 229; Johnson, 1986, pp. 272-74.

20. Egan, 1988.

21. NLRCCAP, 1981.

22. Steiner, 1981, pp. 145-52; Hardin, 1983; Bremner, 1983b, pp. 95-97.

23. National Council of Juvenile and Family Court Judge, et al., 1987, p. 7.

24. Miller, 1987.

25. Romanofsky, 1978, II, 456-60; National Child Labor Committee, 1984.

26. Children's Defense Fund, 1987; Ross, 1983, 175; Poole, 1987.

27. Committee for Economic Development, 1987, pp. 1, 3.

28. Ibid., ix-x.

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WORKING DRAFT

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CASH COWS AND SACRED COWS: COMMERCIAL ACTIVITIES IN THE NONPROFIT SECTOR

by

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We will go into any business but the oldest.

-- Frank Mankiewicz, announcing National Public Radio's intention to pursue for-profit business ventures to offset federal budget cuts.

The pursuit of commercial revenue by nonprofit organizations is a much discussed if not uniformly lauded activity within the philanthropic and public policy worlds. Managers of nonprofit organizations seek sources of reliable and abundant funds -- cash cows[1] -- that will replace dwindling government funding so that they can devote their full attention and resources to the organizations' central goals. At the same time, they want to maintain the philanthropic character of their organizations and the economic perquisites that accompany that character: they want to remain sacred cows and preserve the donative support that they receive from the public and the tax exemptions that they obtain from government.

Commercial activity appears to blur the distinction between business and nonprofit realms. To the general public that equates nonprofit organizations with charity, commercial activity is at least incongruous, if not inappropriate. To the scholar attempting to discover the basis of the division of labor between the nonprofit, government and business sectors, the pursuit of earned income adds a layer complexity to the requisite analysis.

Most of the published examinations of this topic are confined to prescriptions of managerial how-to's, policy analyses of the equity of competition between nonprofit organizations and for-profit firms and considerations of whether or not commercial activities represent a viable source of funding for nonprofit organizations. Little of a theoretical nature has been written which examines the role of this activity from an economic or political perspective. The scholarly literature that attempts to explain why some services are supplied by conventional businesses organizations, some by government bureaucracies and others by the nonprofit organizations has not focussed on commercial activities.

In this paper I examine the existing models of the nonprofit sector to see how well they account for the apparent anomaly of commercial activity. I argue that the models best equipped to explain commercial activity are those which emphasize the cross-subsidizing character of nonprofit activity (i.e., the use of revenues from one activity to support another). However, I find that the role of politics needs greater emphasis both at the organizational and sectoral level if the current models are to be successful.

In a sense this paper only amends and reorders portions of the existing theories of nonprofit organizations. It is an argument that political factors -- never entirely absent from discussions of nonprofits -- are at the core, rather than the periphery of what nonprofits are about. In other words, nonprofits are not well characterized as service organizations unimportantly different from their for-profit analogues.

With respect to commercial activities, the political character of nonprofits has three dimensions: (i) the ideologically-driven behavior of nonprofits at the organizational level that generates the "mission-oriented" character of many nonprofits, (ii) the impact of macro-political phenomena such as changes in national policy and institutions on the incentives and constraints facing individual organizations and (iii) the efforts of nonprofits to influence policy bearing on them.

I highlight the political factors because the dominant approach to the analysis of nonprofit organizations -- economic modeling -- underemphasizes this dimension of the sector. This is not entirely accidental. Economic analysis views markets and economic exchange as normatively, substantively and methodologically prior. That is, normatively, markets are, ceteris paribus, superior forms of social organization. Substantively, markets are seen to be the predominant form of social organization and finally, methodologically, institutions and social interaction are thought to be most productively analyzed as if they were economic transactions. As such, it is not surprising that economic models view nonmarket institutions as residual entities: nonprofits fill in where the market fails. Similarly, politics is of concern where economic factors are insufficient explanation.

I began my analysis with a simple taxonomy of nonprofit commercial activities. I then outline some of the economic models of nonprofit organizations and examine the extent to which they capture the role of commercial activities. I discuss the role of politics in theories of political economy and of the nonprofit sector. I show how commercial activities are best understood against the background of changing national policy. I conclude by discussing the implications of my recasting of nonprofit theories for public policy.

Commercial Activities

Broadly speaking, there are three categories of commercial activities: unrelated business activities, fees-for-services and related commercial activities.

Unrelated business activities -- The goal of these activities is unrelated to the basic mission of the nonprofit. The key purpose is the subsidization of the basic mission through the pursuit of profits in the market. While unrelated business activities are not associated with the direct accomplishment of the mission of the nonprofit, they may be intimately related to its particular competencies. That is, nonprofits will often choose business ventures that exploit their organizational expertise or piggyback on their existing physical capital (Nielson 1986). For example, if a nonprofit organization has facilities that go unused during certain time periods, those facilities may be used to generate revenue. The off-peak use does not further the mission of the nonprofit organization, but it can be an efficient use of those facilities.

Fees-for-services -- The services in these instances are mission services, but unlike classic charities,[2] the recipients of the services are also the source of financial support. Many traditional nonprofit organizations charge for their basic services and more and more nonprofits are beginning to move in this direction. Income from fees for services is sometimes labeled program service fees.[3] University tuition and fees for psychological counseling or job training fit in this category.

Related commercial activities -- These activities are the source of much of the current political controversy between nonprofit organizations and small business, especially as it regards the tax code. They are services which accomplish auxiliary purposes of a nonprofit organizations; typically, related commercial activities are performed to serve the various constituencies of a nonprofit organization. These sorts of activities range from university-operated laundries to museum gift shops to the YMCA's health clubs.

Note that Hansmann (1980) has developed a nomenclature for nonprofits that should not be confused here. He labels nonprofit organizations that receive most of their funding through contributions as donative nonprofits and those that receive most of their funding through fees-for-services as commercial nonprofits. I use commercial activities to designate a broader group of nondonative financing sources but follow his terminology when referring to nonprofit organizations.

Nonprofit organizations can perform their commercial activities either through an arms-length subsidiary or directly under the auspices of the nonprofit itself. Frequently, entirely unrelated business activities are performed in subsidiaries. Clearly, fees-for-services take place without the establishment of a subsidiary because the services constitute the very mission of the nonprofit.

Economic Theories of Nonprofit Organizations

For those that ponder the proper boundary between the public and the private domains, nonprofit organizations stand as an anomaly: they are private organizations explicitly performing public tasks. This anomaly attracts the interest of economists and they have developed most of the synoptic analyses of the nonprofit sector. They are intrigued and puzzled by the existence of non-business, non-governmental organizations operating in the economy. Their efforts to analyze nonprofit organizations using neoclassical microeconomics places them squarely in the midst of debates in political economy. In bringing their disciplinary tools to bear on nonprofit organizations, they are explicitly characterizing as economic entities what many people would consider to be nonmarket institutions.

Economic Models Applicable to Commercial Activities. The theories developed by economists to explain nonprofit organizations are roughly of two types: those that seek to explain the role that such organizations play in the economy and society; and those that seek to identify and account for the distinctive types of behavior in which such organizations engage (Hansmann 1987). Some economists describe these two types of theories as addressing the demand for and supply of nonprofit organizations, respectively.

Among the theories that try to explain the social role of nonprofits, a dominant approach is that of contract failure. The major proponent of contract failure theory is Henry Hansmann. He argues that:

> ...nonprofits arise in situations in which, owing either to the circumstances under which a service is purchased or consumed, or to the nature of the service itself, consumers feel themselves incapable of accurately evaluating the quantity or quality of the service that a firm produces for them (1987, 29).

Because nonprofit organizations face a nondistribution constraint, that is, the prohibition on the distribution of net earnings to individuals that formally control exercise control over the organization, they are appropriately structured to provide such services. A for-profit firm has both the opportunity and incentive to exploit the customer in these circumstances. Because of the nondistribution constraint, a nonprofit organization lacks the analogous opportunity.

According to Hansmann, a consumer or "patron" of nonprofit services is the donor in the case of a donative nonprofit, and the customer in the case of a commercial nonprofit. The donor in making a contribution to a nonprofit organizations, in effect, purchases goods or services for a third party, the beneficiary.

In applying the notion of contract failure to commercial nonprofits, Hansmann cites three factors which might contribute to failure were it not for the nondistribution constraint. First, the service might be complex and difficult to evaluate. Second, the service user may not be the service purchaser -- as with all donative nonprofits, the commercial nonprofit in this case is supplying a service for third party purchase. Finally, the services may be continuing and long-term with the result that the costs of switching providers ("exit") and thus disciplining them is high.

Note that according to the contract failure theory, the nondistribution constraint resolves problems of market failure due to asymmetric information for both donation and fees-for-services. The implication is that commercial nonprofits providing services on a fee basis are not any less legitimately nonprofit than traditional donative nonprofit organizations. Thus, Hansmann's theory readily accommodates one of the three sorts of commercial activity under consideration in this paper. It does not provide as ready an explanation for cash cows.

James (1982) offers a sophisticated analysis of the behavior of nonprofits that is compatible with Hansmann's theory.[4] She characterizes nonprofit organizations as consumer-producer hybrids. In this model, nonprofits engage in a variety of activities, each of which has a different utility and profitability to the organization. The activities fall into three combinations of utility and profitability. Some activities yield positive marginal utility, but negative profit to the organization. They are deficit-producing. A second class have negative utility but produce a profit. Finally, some activities also yield profit but are of neutral utility. The first category is the set of activities which form the crux of nonprofit charitable endeavor -- those services which cannot support themselves in the marketplace. James describes them as implicit consumption, that is, the nonprofit organization's raison d'etre is to perform these activities because the members of the organization enjoy the work, obtain social legitimacy or kudos for their efforts or simply satisfy an altruistic impulse.

The two other types of activity -- which are profitable -- cross-subsidize the implicit consumption. Those activities with negative marginal utility will decline under a variety of circumstances; basically, any time the nonprofit organization can find other means to support its loss-making activities. The cross-subsidizing activities with neutral utility, however, will continue with less sensitivity to changes in the behavior of the first two types of activity.

Rose-Ackerman (1987) elaborates a model which by focusing on the relationship between donors and managers of nonprofits, provides the framework for showing how nonprofit managers may choose to pursue commercial activities as against other funding sources. She suggests that the managers are more interested in the choice of product mix that their organizations produce than are their for-profit counterparts. Nonprofit managers are not as directly responsive to their clientele as for-profit managers in part because of the selective recruitment of certain types of people into such positions in nonprofits: ideologically-oriented professionals gravitate to these positions.

Rose-Ackerman argues that her model explains why nonprofits seek to replace revenue losses caused by government cutbacks. If nonprofit managers were not ideologically motivated, that is, if they simply maximized revenue or output rather than some dimension of service quality, they would always be seeking new revenue sources. The criterion for their search in that case would be the marginal productivity of fundraising. If, on the other hand, service quality is important, fundraising or output may not be maximized if it leads to a decrease in quality.

The character of the output will respond to the character of the revenue: if an unconstrained revenue source declines in availability, the nonprofit will be forced to shift to one with more strings attached. The service mix will change as a result. Rose-Ackerman views government funds as a revenue source without strings attached. She therefore views the funding environment of the 1980s as one in which nonprofits face more constrained funding sources.

This model suggests that commercial revenue will be pursued when (i) its pursuit is relatively lucrative (i.e., high marginal return) and (ii) it is relatively less constraining on the output the manager seeks to produce than other sources. In the face of low but positive marginal return, managers may choose to devote their resources to service quality instead of pursuit of revenue. This model can be viewed as an elaboration of the utility/profitability model of James. The dependency focus in Rose-Ackerman's work arises because her model emphasizes the sensitivity of service mix to the character of funding sources.

It is interesting to note that in the models of nonprofit managerial behavior suggested by James and by Rose-Ackerman, the activities which the nonprofit organization uses to subsidize its deficit producing activities need not be for-profit ventures. For instance, the set of examples that James uses to illustrate her model includes both situations where the subsidizing activity is unrelated to the organization's mission and instances where the subsidizing activity is centrally and uncontroversially related to the organization's mission. An example of the latter is James's analysis of the relationship of undergraduate to graduate education in universities where she argues that undergraduate education produces a surplus which supports the cost of graduate education (1982, 11-12). Note that the subsidizing activity is a conventional, nonbusiness source of income in this case. The commercial character of the subsidizing activity is irrelevant to these models.

The behavioral, supply-oriented models developed by James and Rose-Ackerman are not incompatible with the contract failure and other demand/role models but they are different in emphasis. The supply models ask how nonprofit organizations differ in behavior from other sorts of organizations and how legal and other constraints stimulate those distinctive behaviors. By asking what goals the operators of nonprofit organizations pursue -- what they maximize -- the supply models highlight negative and positive characteristics of nonprofits. On the one hand, supply models stress the potential productive inefficiencies of nonprofits insofar as nonprofits are insulated from the market and therefore allow nonprofit operators to maximize perquisites, budgets, output, status or other ends may not be correlated with efficiency or public goals. On the other hand, the cross-subsidization models which I have reviewed reveal the organizational means by voluntary redistribution is accomplished.

The demand models, in contrast, typically start with a larger unit of analysis, often focusing on sectoral differences. The demand models also differ in their treatment of commercial nonprofit organizations, that is, those nonprofits that charge fees-for-services. The demand models explain, and to a limited extent, legitimate the nonprofit status of such nonprofits as a response to market failure. In contrast, models based on cross-subsidization provide neither an account of why these sorts of organizations are nonprofit nor a normative rationale for their status and tax treatment.

Another way of viewing these differences is to say that the cross-subsidization models (potentially) put redistribution at the center of consideration whereas the contract failure models view redistribution simply as one preference exercised in the market. The cross-subsidizing behavior could be taken as a normative criterion for nonprofit status or at least for tax subsidy. It would then entail a critical stance towards nonprofits which rely wholely on fees-for-services because they provide no services needing subsidy. I discuss the normative question of commercial nonprofits in the context of the controversy over competition between small business and nonprofit organizations in the final section.

Allocative and Non-Allocative Exchange. In addition to the specific limitations that the various economic models face in accounting for commercial activities, there are broader difficulties that these models pose for the analysis of nonprofits and their cash cows.[5] The functional characterizations that Hansmann and James provide for nonprofit organizations transform those organizations into a species of market organization. It is that accomplishment that underlies the impression that the reader gets of the blush being removed from these organizations. To put it crudely, donations to CARE are just purchases of hunger relief. They are one among innumerable kinds of market transaction. The way to evaluate them, therefore, is in terms of their allocative efficiency.

The economic models discussed in this paper characterize nonprofits as allocative mechanisms. I think that it is clear that some nonprofits are redistributive mechanisms. The confusion here is analogous to conflating the allocative activities of the government (i.e., economic transactions viewed from the perspective of optimal use of resources or Pareto-efficiency) such as garbage collection with the redistributive ones (i.e., transactions viewed from the perspective of equity) such as progressive taxation or welfare services.

It may be legitimate to evaluate the allocative dimension of donative nonprofits but that is not the same as claiming that they exist to perform allocative functions. Consider Hansmann's characterization of donations as third party payments for goods provided to more or less irrelevant beneficiaries. For Hansmann, the important characteristic of the nonprofit is that it allows exchange to be made -- the donor exchanges money for the execution of charitable services -- with the reasonable assurance provided by the nondistribution constraint that the donation will not be pocketed. The beneficiary is virtually absent here. But suppose that we focus instead on the beneficiary by concentrating on the subsidized output of the organization. A donative nonprofit typically provides either less-than-market-price goods and services or zero-price goods and services. As James's model indicates, the conduct of a nonprofit can only be understood by placing its cross-subsidizing behavior, the behavior that is mostly likely to be redistributive, at the center of the model. While Hansmann's model is not set up to account for behavioral variation among nonprofit organizations, that difference in orientation does not vitiate the problem that it faces in even beginning to account for important changes in nonprofit behavior such as when a nonprofit begins to charge clients for services it previously provided for free.

Subsuming redistributive functions under allocative characterizations -- by making them a preference exercised through exchange by nonprofits -- obscures important political issues. The growth of for-profit activities among nonprofit organizations can be seen as a rise in the preponderance of cross-subsidization as a funding mechanism for the delivery of public services. Analysis of the sort that is suggested by James's model illuminates questions of market distortion through non-cost based pricing or of the fairness of cross-subsidization for the customer purchasing the subsidizing service. It is not conducive, however, to the examination of shifts in the structure of the welfare state of which this is clearly an important part.

More broadly, charity can be described as voluntary redistribution. Viewing nonprofits as allocative institutions effectively denies a place for altruism. While this approach seems more hard-nosed and realistic, it denies common sense perceptions that altruism is not simply the exercise of one preference among many. More importantly, it prevents the consideration of issues such as whether nonprofits are a means of inhibiting greater redistribution (e.g., coercively through governmental means). For example, the history of private foundations and philanthropy in the US is fraught with acrimonious debate over the legitimacy of the exercise of private power for public purposes (Simon 1978; Nielsen 1972; Ylvisaker 1987). Similarly, the very existence of corporate foundations raises questions of whether corporate and private philanthropy functions to provide reform in place of fundamental social transformation. The characterization of nonprofits as redistributive permits the connection of the study of nonprofits with that of positive and normative issues of distributional justice. Should redistribution be accomplished through private voluntary means? What are the implications of a major change in the nature of that private voluntary mechanism?

This is not to argue that nonprofits are primarily redistributive social mechanisms. Many types of nonprofits are not: their services do not shift resources from the more well off to the less well off. Arts organizations, such as operas and symphonies, have upper-middle class and upper class constituencies and trustees. Universities are viewed by many as functioning to socialize elites. Even many social welfare organizations such as mental health centers are not redistributive.[6]

Keeping redistributive issues in center of analysis of nonprofits has policy implications as well as theoretical importance. In the current controversy over competition between nonprofit organizations and small business, the justification of nonprofit commercial activity hinges on the legitimacy of nonprofit cross-subsidization. Characterizing cross-subsidization only as allocative hinders rather than helps the process of establishing normative standards for nonprofit behavior.

This problem is manifest in more concrete form in that neither James's nor Rose-Ackerman's model tells us why large-scale commercial activity did not occur prior to the 1980s. If, as James's model indicates, it is in the very nature of nonprofits to cross-subsidize internally, then why have they not always done so? Rose-Ackerman's model suggests that any revenue source may be left unexploited if the trade-off between constraint and funds is too unappealing. Absent some specification of nonprofit managers' preferences, this formulation becomes tautological: commercial revenues are not pursued because other funds were available or the commercial revenues were not worth the constraints on managerial prerogatives.

Politics, Policy and Nonprofit Commercial Activity

I want to argue in this section that politics and policy importantly shaped the macro-environment in which nonprofits evaluated their funding options. Neither cross-subsidization, cash cows nor nonprofits in general can be understood without bringing politics and policy into the story.

There are two different ways in which politics and policy shape nonprofit commercial activity. First, government policy can directly and/or deliberately shape the sectoral division of labor. I will review the recent theories of Salamon (1987) and James (1987) in which government-nonprofit relations are made a more central determinant of nonprofit roles. Second, government action taken for essentially unrelated reasons can affect intersectoral relationships.

The emphasis on politics and policy and the associated focus on the way in which government can structure behavior in society in often unintended ways is related to some arguments now being made by neo-statist political theorists. Neo-statists are interested, in the words of recent book, in Bringing the State Back In (Evans, Rueschemeyer and Skocpol 1985). Their program has two components. First, they argue that the state is frequently autonomous, that is, it is capable of formulating and pursuing goals that are not simply reflective of the demands and interests of social groups, classes or society (Evans, Rueschemeyer and Skocpol 1985, 9). It is not my intention to argue that the American state was or is crucially autonomous with respect to government policy on nonprofit organizations or cash cows.

Second, they propose that states be studied from a "Tocquevillian" perspective:[7]

government rather than in competition. He describes the respective roles of government and nonprofits as policy formulation and policy delivery and he adduces a variety of historical evidence to indicate that such a complementary relationship can be dated back to pre-revolutionary times in the United States (1987, 101). The evolution of the respective roles in public service has been from provision by nonprofits to provision by government.

The shift in responsibilities has arisen not in response to government or market failure as other theorists have claimed but in response to the inadequacies of nonprofit provision. Salamon labels such inadequacies voluntary failure and specifies four sorts of failure: philanthropic insufficiency, philanthropic particularism, philanthropic paternalism and philanthropic amateurism. He also discusses the strengths of nonprofits vis-a-vis governments thereby explaining the benefits gained by collaboration. But it is the account of the shift of provision from nonprofits to government that is interesting here because of its relative novelty among theorists of the nonprofit sector and because of its historical verisimilitude.

Salamon combines the explanation for the growing role of the state with the differentiated characterization of government and nonprofit roles to arrive at a theory that avoids ascribing a residual role to nonprofits. It is a theory that makes sense of the current character of nonprofit funding with its dependence on government funding and its surprising lack of donative support.[9]

Estelle James, in recent comparative international study of nonprofit sectors, has been led to amend the economic emphasis on nonprofit organizations as a response to market failure as well. Like Salamon, she finds differentiated roles for nonprofits and government: "whereas government is a substitute for NPOs [nonprofit organizations] in production, it is a complement in financing" (1987, 397).

James posits two variables which explain why certain services are provided by the private sector rather than government: excess demand and differentiated demand. The former occurs where citizens find certain (typically quasi-public) services underprovided by government and turn to private production to obtain those services. The second demand-side explanation, differentiated tastes, occurs where government production is constrained due to the differences in taste with regard to the kind rather the quantity of services. James specifies four conditions under which private sector production would grow:

> 1) peoples' preferences with respect to product variety are more heterogeneous and more intense, owing to deep-seated cultural (i.e., religious, linguistic, ethnic) differences;
> 2) this diversity is geographically dispersed so it cannot be accommodated by local government production;
> 3) government is constrained to choose a relatively uniform product; and
> 4) the dominant cultural group is not determined to impose its preferences on others; hence private production is a permissible way out. (1987, 402)

James then goes on to argue that private production typically occurs under nonprofit rather than for-profit auspices primarily because ideologically-motivated groups and individuals, especially those affiliated with organized religion, seek to maximize their adherents. The nonprofit form allows for behavior not compatible with profit maximization. For example, below cost provision of educational services attracts pupils and is only possible with an organizational form that is conducive to cross-subsidization. Other factors such as access to low cost labor, client trust and loyalty due to ideological affiliation and government subsidy secured through exercise of political power cement the advantage that the nonprofits have over for-profits in provision of the relevant services.

> In this perspective, states matter not simply because of the goal-oriented activities of state officials. They matter because their organizational configurations, along with their overall patterns of activity, affect political culture, encourage some kinds of group formation and collective political actions (but not others), and make possible the raising of certain issues (but not others). ... When the effects of states are explored from the Tocquevillian point of view ... the investigator looks more macroscopically at the ways in which the structures and activities of states unintentionally influence formation of groups and the political capacities, ideas, and demands of various sectors of society (Evans, Rueschemeyer and Skocpol 1985, 21).

This aspect of the neostatist approach holds out the potential for explaining what nonprofits and their cash cows have in common in spite of the diversity of industries in which they operate. From this perspective, nonprofits and cash cows need not share functional characteristics in all times and all sectors. Instead, their commonality can grow in response to benefits bestowed or penalties threatened by the state (e.g., tax exemptions or its withdrawal). Organizations can consciously assume the nonprofit form in response to the incentives provided by the state. And those incentives can change over time as the larger political economy and specific government policies evolve. The government policies that so shape the development of nonprofits and cash cows need not be responses to market failure and therefore need not be driven by autonomous economic factors.

There is another way in which the state may be crucial to the analysis of nonprofit organizations. Most theories of the institutional division of labor start with the question: why not the market? The answer is typically one variant or another of market failure. While the characterization of certain goods and services as not being amenable to market provision because, say, they are public goods[8] may be transhistorical or transcultural, government and other institutions can play a crucial role in altering the environment in which the good is produced or consumed so that it may capable of being provided through marketplace means.

Karl Polanyi propounded a thesis related to this in The Great Transformation when he argued that the establishment of free wage labor markets in the 18th and 19th centuries was not a natural development but rather the result of protracted political struggle and deliberate institutional change (1944). By the same token, the character of goods and services may be altered by public policy so as to change the characteristics that make them less amenable to market provision.

Similarly, markets do not function where the consumers lack the income with which to make purchases. In order for their needs or demands to be met, they must be subsidized in some manner. The cross-subsidization that occurs within nonprofits is one way to remedy those needs. Government subsidy of providers is another. And direct government subsidy of the consumers is a third. The point here is that government has the potential for shifting sectoral assignments through changes in the methods of subsidization. While answering the question "why not the market?" is illuminating insofar as it tells us that some goods are not amenable to marketplace provision, it avoids the larger question of why the character of those goods evolve.

Theories of Nonprofit-Government Relations. Before turning to the discussion of the specific political phenomena that influenced nonprofit commercial activity, it is useful to look at the theories that model nonprofit-government relations. Salamon (1987) and James (1987) both argue for a revision of economic theories of the nonprofit sector which characterize the sector as a residual set of institutions arising as a result of the failure of either the market or the government to meet social needs.

Salamon maintains that nonprofits historically existed in partnership with

James explains government delegation and subsidization of nonprofit provision by the cost advantages obtained by using nonprofits which have access to low cost labor and multiple funding sources. She also argues that various social groups will want to control provision of certain services for ideological reasons (e.g., religious groups may want to control schooling because it is a means of socializing new members of the faith) and such groups may form coalitions to obtain the subsidies.

These two models place the nonprofit-government relationship in the center of theorizing about the nonprofit sector. Salamon's account with its greater verisimilitude turns the tables on the economists by posing the question: why not nonprofit organizations? His theory lacks a substantive theoretical discussion, however, of nonprofits versus for-profits. One could impute a market failure component similar to those used in the other models discussed in this paper with a Polanyian perspective: social services are not amenable to for-profit provision; why and how they become amenable to certain sorts of provision is importantly a function of government and nonprofit action.

James's model builds on her earlier analysis of cross-subsidization in that it relies on ideological components in the development of the supply of nonprofit services. In her older model this would be called organizational consumption. The later model is much more sophisticated in that it posits ideological interests on the part of consumers and it characterizes government as more than a competing multi-product nonprofit organization.

Against the background the economic and political theories of the nonprofit sector sketched above, I want to now review some of the concrete developments in national policy and in the nonprofit sector that have contributed to the emergence of increased commercial activity. The phenomena that I describe will evince a clear role for the impact of politics and policy on nonprofits and their cash cows.

Four political phenomena shape commercial activity of nonprofits:

1) government funding of nonprofit organizations and the resulting expansion of nonprofit sector and the incursion of for-profit firms into traditional nonprofit industries;
2) privatization and the contraction of the nonprofit sector;
3) tax policy; and
4) controversies over competition between business and nonprofits.

I will treat the first three phenomena in the remainder of this section and the fourth in the concluding section on policy implications.

Government Funding and Expansion of the Nonprofit Sector. Increases in government spending on social services (in the broadest sense of that term) had two very important impacts on the nonprofit sector and on the sectors' commercial activities. First, increases in government funding of nonprofits in the postwar period stimulated the growth of the nonprofit sector. New organizations were created in response to this stimulus and existing organizations expanded. When, several decades later, the Reagan Administration reduced that funding, the organizations threatened by those cut-backs sought new revenue sources to replace government funding. Commercial revenue was one source of alternative funding.

Second, in a variety of social and health care fields, the government initiated extensive third-party, voucher-type financial support of services in industries where nonprofits were active. In other words, the government gave individuals money with which to buy services from providers that were either nonprofit, for-profit or governmental institutions. The most notable of these programs is Medicare, the federal health insurance program for the aged. Client populations that previously had only been served through subsidized provision by nonprofits or the government could now be served by for-profit firms. The

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provider organization no longer needed to obtain and furnish the subsidies on behalf of the clientele; the clientele brought the subsidies with them. The result was that in a number of industries it was now profitable for conventional businesses to compete with traditional nonprofit social service and health care providers. Competition between nonprofits and business resulted. Political controversy followed.

The effects of increases in government funding, thus, produced political and economic repercussions that are central to the circumstances that shaped the pursuit of revenue by nonprofits in the 1980s.

Nonprofit organizations providing personal social services began to obtain a significant portion of their funding from the government in the 1960s. In particular, the 1967 amendments to the Social Security Act, which provided grants that matched triple the value of funds donated to nonprofit social service agencies increased both nonprofit reliance on government funding and the size of this portion of the nonprofit sector. Nonprofit social service agency reliance on government funding was further increased in 1974 when Title XX of the Social Security Act broadened the criteria for eligibility for receipt of personal social services (Kramer 1982).

Similarly, the Educational Television Facilities Program and the establishment of the Corporation for Public Broadcasting in the 1960s stimulated the growth of nonprofit broadcasting.

Public subsidy stimulated the growth of nonprofit health care providers in several ways. Direct funding of providers that served the poor just after World War II spurred nonprofit growth as did the system that replaced it: Medicare and Medicaid. These programs subsidized the patient directly and the provider indirectly by stimulating demand. As will be discussed below, this form of support also encouraged for-profit provision.

Some federal health care funding was designed specifically to stimulate the growth of nonprofit institutions. The Hospital Survey and Construction Act of 1946, known as the Hill-Burton Act , subsidized a variety of nonprofit and public health care facilities especially short term general hospitals (Marmor et. al. 1987, 226; Starr 1982, 348-351).

Privatization. Privatization has a double importance to the analysis of cash cows. As an empirical matter, withdrawal of government funding stimulated nonprofit commercial activity. As a theoretical and ideological matter, it signals an attempt to alter the institutional division of labor in American society. But it also exposed significant ignorance, even misunderstanding of the character of the nonprofit sector.

The proponents of privatization view nonprofits as an alternative to the state. Earlier, I discussed Salamon's theory of government-nonprofit partnership. His theory grows out of the findings of the Urban Institute's Nonprofit Sector Project which he directed. The Urban Institute has been studying the changing role of nonprofit organizations in the US and especially the relationships between these organizations and government in a large scale research project for the past 6 years.

The Urban Institute research captured a crucial characteristic of the situation posed by federal budget cuts for nonprofit organizations: they were getting caught in a squeeze. On the one hand, the government was explicitly looking to them to step in and provide those services which were being eliminated from the federal budget. This stimulated demand for nonprofit services. On the other, federal financial support for nonprofits was being reduced -- the supply of nonprofit services was thus being curtailed. Finally, the amount of the shortfall was much larger than could be expected to be met by increased donative support of nonprofits.

This research had two great strengths. First, it recognized as few other analyses of the sector had, that nonprofits received a significant portion of their funds from government and that federal budgets would have direct impact on them. Second, it quantified the magnitudes of the various impacts.

As of 1981, government was the largest source of funding for the sector constituting 41% of revenues. Of the ten subsectors that the project analyzed, six relied more on government revenue than more than all other sources combined and for eight subsectors government was the largest single source of revenue. In none was donative support the largest source of support.

Thus it is not surprising that the budget cuts in the period 1982-1986 produced revenue losses to nonprofit organizations (exclusive of Medicare and Medicaid) of approximately $23 billion below what would have existed had FY 1980 spending levels been maintained. That translates into an approximate annual loss of $4.6 billion dollars a year in "supply." In the same period, cuts in areas in which nonprofits are active have amounted to about $70 billion. This has generated the increased demand for service provision by nonprofits.

Private philanthropy was expected to make up the gap between supply and demand in the support of health, welfare, culture and the arts. The Urban Institute's research indicates that private giving was able to make up for some of the budget cuts but giving could not do the whole job. Charitable contributions made up for only 57% of the direct revenue losses sustained by nonprofits and only 7% of decrease in government spending in the areas of interest to nonprofits. Looking to the future the Urban Institute calculated that in order to offset the budget cuts that the administration has proposed for FY 1987-1989, private giving would have to grow at a rate of 700 to 800% higher than its peak rate in recent years to meet the service gap. To offset the direct revenue losses, giving would have to grow at a rate 200% to 300% higher than its recent peak rate.

This combination of increased demand, decreased federal revenue and limited growth in private giving is compounded by the recent revision of the tax laws. The new flatter tax rates decrease the economic incentives for charitable giving. At the same time, the abolition of the charitable deduction for nonitemizers and the increase in the floor for itemizers further reduces tax incentives for giving. Nonprofits have been getting squeezed all around.

The Urban Institute's findings demonstrate that nonprofits had relied on government support and that cutbacks in that support put them in a position where they had great incentive to seek alternative sources of revenue. It is not surprising that this pressure lead many of them to pursue commercial revenue. Here it is important to note that it is not the "comparative advantages" of the respective sectors that generates the intersectoral division of labor. Instead it is the organizational response to macro-political changes -- large scale federal budget cuts -- that produced the result in question.

Tax policy. Tax policy is important to the discussion of cash cows for three reasons. First, the major portion of government policy on nonprofit organizations is accomplished through tax policy. There is some policy is that realized through administrative regulation of nonprofits receiving government grants and contracts and some is achieved through state laws establishing the requirements for incorporation of nonprofit organizations. Nonetheless, most policy, especially policy on commercial activity, is a matter of taxation.

Second, as the chief means of government oversight, tax policy regarding cash cows is the locus of political dialogue over the legitimacy of commercial activity. That dialogue as recorded in congressional testimony, court cases and ancillary documents is, unfortunately, the only significant source of historical information on the pursuit of commercial revenue by nonprofits. In this respect tax policy is important, not for itself, but as a vehicle for historical inquiry.

Third, tax policy limits and shapes the types of commerce that nonprofits can pursue and it effects the potential profitability of that commerce.

Broadly speaking, tax treatment of commercial activities has taken two forms: the destination test prior to 1950 and the relatedness test from 1950 onward. Not surprisingly, not until the income tax became an important part of the fiscal landscape with the establishment of the national permanent income tax in 1913 (Witte 1985) did tax treatment of nonprofits and of cash cows become a political issue. Major policy on the tax treatment of cash cows was first established in 1924 in a Supreme Court case, *Trinidad v. Sagrada Orden de Predicadores* (263 US 578). In a case concerning a Philippine[10] religious order which used rental income from substantial landholdings and sales revenue from articles sold to churches and related institutions, the Court found such income to be tax exempt because of the use to which it was put. According to the destination test, as this criterion was called, the taxability of income from commercial activities carried on by nonprofits was exempt as long as that income was used for charitable purposes. The *destination* rather than the *source* of the income was determinative.

It is important to understand that corporate income is now and was at the time of the *Sagrada* decision, taxed twice. First, the corporation pays taxes on its net income. Then, shareholders pay taxes on the dividends. According to the destination test, nonprofit organizations owning and operating businesses paid taxes at *neither* point. Regardless of the exemption test used, however, the second level of taxation is nonetheless generally avoided if the shareholder is a nonprofit organization.

By the early 1940s, both the Treasury and the Bureau of Internal Revenue (the predecessor to the IRS) were starting to object to the destination test and to consider the tax revenue and social policy implications of allowing charities to be extensively involved in business activities (Blodgett 1946, 420).

What brought cash cows to the attention of the public, however, was the Mueller Macaroni case. A group of wealthy New York University Law School alumni purchased the C.F. Mueller Company, the country's largest manufacturer of noodles, macaroni and pasta. The alumni, hoping to provide a source of income which would allow their alma mater to achieve greater prestige in the academic community, acquired the company using techniques that we would now call a leveraged buy-out. While the action differed little from the pre-war cases of nonprofit commercial activity, the reaction here was instantaneous and vociferous. *Fortune Magazine* ("Tax Abuse..." 1950) and *The New Republic* (Mezerik 1950) editorialized about the scandalous behavior of charities and one Congressman thundered that "if something is not done ... the macaroni monopoly will be in the hands of the universities" (House Ways and Means Committee 1950, 580).

But contrary to some accounts, it was not the Mueller case in and of itself that galvanized Congress and the public. The House Ways and Means Committee initiated hearings in 1947 on the conduct of businesses by tax exempt organizations. Congress was concerned about cash cows several years prior to the hubbub over Muellers. Even representatives of the nonprofit sector were curious about the extent of commercial activity within their domain.

One form of nonprofit commercial activity which most observers found especially vexing was sale-leaseback of real estate. According to Congressional testimony (House Ways and Means Committee 1950, 176; Senate Finance Committee 1950, 560-66), colleges and universities were involved in extensive sale-lease back operations with department stores. For example, in the first widely publicized case, Allied Stores sold the real estate associated with some of its operations to Union College. The college then leased the property back to the department store. In such transactions, the property was typically sold at above market costs which the nonprofit organization recouped because it paid no real estate taxes or income taxes on the transaction. The department store benefited both from an above market sales price, a below market rental rate and the deductibility of the rental payments.

This arrangement spread rapidly and by 1950 Yale had sale lease-back arrangements with Macy's in San Francisco and Frank & Seder in Philadelphia; Harvard with Gimbel's; Oberlin College with Montgomery-Wards, Sears, and Woolworth's; and the University of Pennsylvania with Lit Brother's in Philadelphia.

Public ire was generalized and unspecific. Many of the abuses cited were instances of businesses establishing charities or foundations in order to maintain control of corporations in the face of estate taxation or simply to avoid taxation. These cases were conflated with instances where operating nonprofits such as universities pursued commercial revenue.

The policy concerns of Congress centered on two issues: the potential that tax exemption gave nonprofits unfair competitive advantage over taxable businesses and the loss of tax revenues engendered by the removal of industrial and commercial activities from the tax base. I will discuss the economic validity of the claim that tax exemption generates unfair advantage in the section on unfair competition below. Regardless of the technical merits of the complaint over unfair competition, Congressmen treated the issue as self-evident and serious.

With regard to the impact of nonprofit cash cows on the tax base, the Treasury estimated that tax revenues of about $100 million were forgone through their tax exemption. Other analysts argued that the forgone revenues were closer to three or four million dollars (Note 1951, 852, 852n9; Senate Finance Committee 1950, 514).

The result of these revelations and of the concern shown by Congress was a fundamental change in tax treatment of nonprofit commercial activity. The Congress established a relatedness test to replace the destination test. Now the standard for taxability was the relatedness of the revenue-raising activity to the nonprofits' basic tax exempt mission. Commercial activities pursued by nonprofits deemed to be unrelated were subject to the unrelated business income tax (UBIT). If such activities were carried out under the auspices of a separate for-profit corporation -- a feeder corporation -- revenues from those activities were fully taxable at the corporate rate.

Few changes of significance to the issues treated in this paper have been made in the taxation of nonprofit commercial activities since 1950. While the tax treatment of foundations was drastically revised in 1969, only technical changes in the relatedness test were made. Some classes of nonprofit organizations, primarily churches, social welfare organizations and a variety of mutual benefit organizations, that had been previously excluded from the coverage of the unrelated business income tax were now covered by that tax. Also, the tax exemption of rental properties owned by nonprofits was further restricted in order to thwart new, more sophisticated versions of the sale-leaseback tax avoidance (Treusch and Sugarman 1983, 244-251). These amendments raised no political interest of the magnitude surrounding the 1950 policy changes. Not until the 1980s with the mobilization of the small business community over the unfair competition issue did this tax policy issue regain political salience.

The battles over taxation of commercial activities are of importance to theories of the nonprofit sector in three respects. First, the vagaries of the tax code provide opportunities for nonprofits to earn revenue and concomitantly, the increasingly stringent treatment of commercial activities limits those activities. Second, attempts by nonprofits to affect tax policy -- either to obtain favorable treatment or to mitigate punitive sanctions provides a link of a political sort between individual nonprofit organizations and the macro-political environment in which they operate.

Third, political conflict between nonprofits and other sorts of institutions and groups such as small business or ideologically motivated factions, imposes a constraint on individual nonprofit organizations' activities. In the models that characterized nonprofit organizations as institutions that engage in cross-subsidization, we saw that there were generally two classes of activities in which the organizations engaged: mission activities and subsidizing activities. From the perspective of those that operate the nonprofit organization, the identity of the latter activities is unimportant as long as they meet certain minimum criteria of profitability and lack of constraints or disutility. In contrast, the identity of the mission activity is important -- it is what motivates the very operation of the organization.

Politics may be integrated into these models by portraying the controversies as the means by which various groups in society either intentionally or unintentionally raise the costs of one of a set of potential subsidizing activities relative to other possible sources of subsidy (e.g., the cost of commercial activities versus the cost of donations). The costs can be raised directly as nonprofit managers find the controversy requires managerial attention or as public disaffection is manifested in decreased financial support. Or the costs may be imposed indirectly through the eventual policy that is implemented.

This is not just idle theoretical rumination. The political strategy of the small business critics of nonprofit organizations explicitly includes a component geared toward changing the public perception of nonprofit organizations in order to influence the profitability of certain sources of revenue (Pillsbury 1987, 39). The "halo effect" is just as much a target as the tax exemptions.

Policy Implications: Competition Between Nonprofit Organizations and Small Business

The controversy over competition between nonprofits and small business provides an opportunity to indicate some of the policy implications of this discussion of commercial activities and nonprofit theory. I want to suggest in this section that while small business substantially misunderstands the nonprofit sector and uses a notion of fairness that is not consonant with the economic theory of taxation; firms competing with nonprofit organizations may be bearing an undue burden of the cost of social and cultural services in the United States.

It is helpful to begin by stating some of the central aspects of the controversy up front. First, generally but not universally, it is small business that is upset about competition from nonprofit organizations. Only in health care, where large investor-owned for-profit chains are competing with large nonprofit chains, does one see big business involved. Second, the major complaint is that nonprofit organizations enjoy tax exemption not available to their business rivals that gives the nonprofits an unfair competitive advantage. Sometimes the complaint is that nonprofits should not be competing at all, regardless of tax exemption. Third, the privileges enjoyed by nonprofit include:

- exemption from federal, state and local income taxes;
- exemption from state and local property taxes;
- exemption from state and local sales taxes, both on sales to and from nonprofits;
- exemption from federal unemployment tax (FUTA);
- exemption from the provisions of the antitrust statutes;
- preferential postal rates;
- exemption from certain aspects of price discrimination, unfair competition, securities, copyright and bankruptcy regulations.

These privileges vary by state and locality as well as by type of nonprofit organizations (e.g., mutual nonprofits enjoy fewer privileges than 501(c)(3) organizations).

Most of the conflict revolves around related commercial activities of nonprofit organizations. Because such activities are related, usually they are tax-exempt. As such, they may be advantaged in the market and their advantage appears to many people to be illegitimate regardless of its material impact or other factors. Related activities also pose a competitive threat to small business competitors because there are often cost efficiencies associated with the conduct of the combination of the related and mission activities. In addition, the nonprofit organizations may have privileged access to clientele that small business competitors find difficult to counter. Universities and hospitals often have captive markets that businesses find inaccessible.

Unrelated business activities are usually less a matter of contention. These activities are taxable either through the unrelated business income tax or through corporate income taxes if conducted through a separate subsidiary. To the extent that they are less intimately bound up with the nonprofit's mission activities they resemble conventional competitors to their small business rivals.

Competition over fees-for-services tends to have a different character than competition of the other two types. For-profit and nonprofit firms can only exist in the same market if the consumers in that market have income with which to purchase the relevant services. The source of that income can be third-party payments, the consumers' own resources if the consumer is not economically disadvantaged or the government if the service in question is purchase of service contracting. Frequently, the nonprofit providers pre-date the for-profit providers in these markets.

Arguments of the Interests. The small business community finds competition from nonprofit organizations both illegitimate and unfair. The illegitimacy stems in their view from the fact that there should be no nonprofits in markets capable of sustaining for-profit commerce regardless of prior circumstances. The unfairness arises from the exemptions and benefits provided through government policy.

Small business advocates make two sorts of claims about the illegitimacy of the presence of nonprofit providers in the market. First, they lament the shift of nonprofit organizations from donative funding to fees-for-services and for-profit activities. Nonprofit organizations obtain their special status, in this view, because they are charities. Second, the purpose of nonprofits is to do what business is incapable or unwilling to do. Therefore, if business finds a market viable that it had previously declined to serve, it is appropriate and fair that nonprofit providers already present in the market face new competition or that the nonprofits relinquish their tax advantages or even that the nonprofits exit that market.

Unfairness is thought to occur because tax and related advantages allow nonprofits to underprice their competitors and to use retained earnings to expand faster or to avoid bankruptcy. In addition, the community good will that nonprofits enjoy is thought to produce a "halo" effect that induces consumers to favor them over their small business competitors. Some advocates insist that they welcome competition from nonprofit organizations but maintain that that competition should be played on a "level playing field," that is, that no competing group should advantaged. Other advocates argue that nonprofits should not be competing at all but since banishing them from the market is politically infeasible, revisions of government policy should reduce the advantages enjoyed by nonprofits. Generally, it is the related commercial activities of large nonprofit organizations in the health care and higher education sectors that is the object of most of the ire of the small business critics.

The remedies recommended by the small business community include tightening the criteria for exemption of commercial income under the relatedness test, improving federal data collection efforts so as to reveal the exact extent of nonprofit commercial activity and increasing the efficacy of enforcement mechanisms and associated penalties (SBA 1987b).

Representatives of the nonprofit sector dispute both the characterization and the extent of the problem. They reject description of nonprofit organizations as exclusively dedicated to service to the poor or as primarily funded by donations. They argue that the socio-economic status of their clientele is appropriately diverse (concentrating on the lower middle and middle classes). Provision of services exclusively to the poor, they assert, would stigmatize the recipients of the services.

Nonprofit advocates also argue that an objective examination of the unfairness of competition would take into account the advantages enjoyed by small businesses, including subchapter S tax treatment[11] and government contract set-asides.

Nonprofit organizations also dispute the notion that nonprofits do not belong in markets where businesses are capable of providing services. Arguing that business firms' provision of services can be erratic because their participation in a market is tied to the vagaries of that market, nonprofits counsel that their long term interest in providing predictable and uninterrupted service to the public be recognized and their need for institutional stability be acknowledged.

Nonprofit advocates claim that existing data do not clearly indicate one way or another whether nonprofits are extensively involved in commercial activity. They say that it is premature to pursue reforms of the tax code in the absence of more definitive data. They particularly disagree with the conflation of for-profit activities with fees-for-services. The combination of data from those two categories inflates the magnitude of the activities considered to be unconventional.

Economic Analysis of Unfair Competition. Economic analyses of the unfairness of competition tend to be rather complicated compared to allegations that nonprofit competition is unfair prima facie. According to an analysis by Rose-Ackerman (1986a), fairness is importantly a matter of foreknowledge and market structure. From an economic point of view no group of firms is entitled to above market returns nor should such a group be forced to endure below market returns for noneconomic reasons that cannot be anticipated prior to investment. If an investor enters a market that he or she knows is characterized by below market rates of return, then there is no unfairness. (There may be inefficiency, but that is a different question.)

There are several concepts from the economic study of taxation that are important to understanding Rose-Ackerman's argument. First, horizontal equity is the basic criterion employed in discussing the fairness of taxation. This principle mandates that entities in similar situations should pay the same taxes.

Second, the incidence of taxes must be distinguished from their burden. The former refers to who is formally responsible for the payment of taxes; the latter to who actual bears the economic burden of the costs of the taxes. If a firm, for example, can pass the costs of taxation through to its customers then the customers sustain the burden while the firm only bears the incidence.

Third, one class of investors may be advantaged through the exemptions that their firms enjoy but if public policy indicates that those advantages are warranted to achieve some social objective then fairness becomes a matter of the legitimacy of the means and substance of collective decisionmaking. If a legislature decides that charities should retain more of their earnings than business stockholders, this may be deemed fair if the means by which this choice is made is deemed fair. This is not a question appropriately analyzed with economic theory.

Rose-Ackerman argues that the two key advantages thought to arise from tax exemption -- opportunity to engage in predatory pricing; and the ability to grow faster and thereby avoid the risk of bankruptcy due to faster accumulation of earnings -- are neither true nor false prima facie. Instead, empirical conditions shaped by market structure, tax laws and the capital market determine whether nonprofit tax exemption forces for-profit competitors to endure below-market returns.

Predatory pricing due to tax exemption is not a valid concern. If lower prices were profitable, for-profits would lower their prices as well. But nonprofits may influence market price without engaging in predatory pricing by entering a market where marginal for-profits are just breaking even. The entry of the nonprofits shifts the market supply curve outward (i.e., it expands the amount of goods and services supplied by the industry as a whole) and thereby lowers prices. If exit is costly for for-profits, they may face lowered prices even if no competitor sets prices below cost.

Similarly, whether or not a for-profit firm is disadvantaged vis-a-vis bankruptcy risks depends on the tax treatment of losses and the availability of capital. Bankruptcy risk is relative risk. This is easiest to see in a situation where demand is unexpectedly low. All firms face risk, but a firm's risk is lower if there are competing firms more marginal than it, because the exit of marginal firms with the smallest reserve of past earnings will increase prices and improve market conditions for the surviving firms (1986a, 42).

Nonprofit organizations can retain more earnings than for-profits, ceteris paribus, because those earnings are not taxed. This increases for-profits' relative vulnerability to bankruptcy. However, that is only true if loss carryover provisions of the tax code are neglected. The greater the carryovers, the smaller the differences there are between nonprofits and for-profits in the ability to accumulate retained earnings and therefore the less difference there is in bankruptcy risk.

Rose-Ackerman draws from her analysis a strikingly counterintuitive finding: unfairness to for-profit firms will be lessened if the unrelated business income tax (UBIT) is repealed. She argues that a tax that would remove unfair advantage is theoretically possible but administratively intractable because it would have to be sensitive to factors such as whether the for-profit firms were enjoying above market returns, whether there was excessive nonprofit entry and whether exit would be costly for for-profit firms. She suggests that absent such a complex tax, the UBIT increases injury to for-profit competitors by concentrating nonprofit business activities in specific lines of business -- those exempt from the UBIT and corporate income tax -- and increasing the likelihood that returns to investment in such a market will be lowered. She suggests that repeal of the UBIT would disperse nonprofit commercial activities across the economy, mitigating the magnitude of the impact of nonprofit competition on individual industries.

Policy Implications. There are both positive and normative implications to be drawn from my analysis of cash cows for the current controversy. To the extent that cross-subsidization is a key feature of nonprofit organizations and that in some way or another nonprofits pursue activities unsupportable in the market, several important inferences can be drawn. First, those nonprofits that support themselves solely through fees-for-services may not be entitled to tax exemption and related public subsidies and dispensations. Their ability to operate solely on the basis of fees-for-services implies that their services lack a redistributive or collective component. This criterion would not disallow exemption for nonprofit organizations that operate partially on the basis of this sort of financing or that employ sliding scale fee systems.

Second, the small business community's attempt to limit nonprofits to donative financing and narrowly charitable activity misconstrues what nonprofits are about currently and historically. If the historical research that is beginning to emerge is correct, pure charities are more a part of American folklore than of the actual American political economy (Hall 1987b).

The discussion of the role of politics and policy in shaping nonprofit commercial activity raises concerns in a different dimension. Advocates of various ideological stripes look to nonprofits to play a vital role in the welfare state. Some conservative privatizers want them to relieve the load on government. Even those not advocating privatization see a crucial role for nonprofits in service delivery, advocacy or constituent participation. As various forms of financial support available to nonprofits are successively curtailed -- government funding, charitable deductions, and now commercial cross-subsidization -- policymakers need to face up to the possibility of the gradual enfeeblement of the nonprofit sector.

This raises an important point about the dispute over fairness. While the dearth of data and the complexity of the requisite analysis makes conclusions hard to come by, it is probably the case that fairness is not a matter of leveling a tilted playing field because the field is not tilted but bumpy. That is, the unfairness may not lie so much in the relative advantages that nonprofits have over their small business competitors -- the magnitude of the nonprofit advantage has yet to clearly established especially in an analysis that incorporates small business tax advantages. Instead, the unfairness may lie in the fact that small businesses are bearing the burden, through depressed market returns, for a portion of the cost of public services that might be more equitably distributed through the general tax system. If nonprofits received more funding through government, or if services provided by nonprofits were provided directly by government, then the cost of those services would be spread through out the tax base rather than being imposed on small business through nonprofit competition. In this sense, small business is bearing an undue portion of the cost of the welfare state.

The policy implications of this perspective on unfairness are complex. First, this perspective relies on the sort of market analysis described by Rose-Ackerman where subcompetitive returns on investment for an industry have to be established. Second, remedies for the inequities that are found could include (i) more direct government funding for nonprofit organizations in order to decrease their incentives to pursue commercial revenue, (ii) a shift to direct government provision of public services, (iii) increases in tax deductions for charitable contributions in order to increase donative funding, (iv) compensation for small businesses hurt by nonprofit competition and (v) an explicit choice to reduce the relevant public services by prohibiting certain sorts of nonprofit commercial activity without providing compensating increases in funding for nonprofits or without increasing government provision.

Some of these remedies have obvious drawbacks. The shift to direct government provision undermines whatever virtues nonprofit provision provides by reducing this sector's role. Compensation for small business is administratively complex and suffers from difficulties of establishing clear and legitimate standards of injury. The proposals for greater government funding or increased tax incentives for giving produce fewer negative consequences but it has been precisely the movement of public policy away from such subsidies that has contributed to the pursuit of commercial revenue by nonprofits. Concern over the federal budget deficit militates against the re-adoption of these approaches. In the short term, it appears that, if small business succeeds in its political quest, the "remedy" employed will be limitations on commercial activity and reduced nonprofit services. We will have both fewer sacred cows and fewer cash cows.

I began this paper by pointing out that commercial activities of nonprofit organizations violate our commonplace conceptions of what nonprofits are about. The apparent anomaly of organizations whose distinctiveness rests in their being unlike businesses, acting like businesses, motivates the two stage process of this inquiry. First, I have asked what exactly we mean by nonprofit organizations and then I have asked how well those answers have accommodated commercial activity.

In order for commercial activity to be an anomaly, there must be a coherent notion of "nonprofitness" against which to measure the aptness of this particular activity. Throughout this paper I have argued that cross-subsidization is an important, perhaps essential feature of both nonprofits in general and of their commercial activities in particular. Cross-subsidization is not unique to nonprofit organizations -- large business firms subsidize one line of business with the profits of another in expectation of future returns from the first, deficit-producing line. However, if economic theory is correct, the capital market constrains the firm's ability to indefinitely postpone the payoff from that money-losing activity. In contrast, the nondistribution constraint isolates nonprofit organizations from the capital market, thereby relieving it of the pressure from investors and allowing it to take on as its *raison d'etre*, activities which cannot support themselves.

Cross-subsidization provides a plausible behavioral account of much nonprofit activity. It is a "supply-side" theory in the terminology introduced earlier. It is less powerful in accounting for demand factors or in explaining the role of nonprofit organizations in society. I cannot provide, at this point, a comprehensive theory of the role of nonprofit organizations based on my analysis of them as cross-subsidizers. I can, however, argue that the behavior in question is more easily understood when the nonprofit sector is viewed against the backdrop of its environment. Some of the models I have reviewed (e.g., James and Rose-Ackerman) have incorporated the impact of the government and business sectors on nonprofit organizations but they generally leave out or under-emphasize the importance of the macro-political environment.

Thus, the analysis of cash cows and the broader study of nonprofit organizations of which that analysis is a part is largely an inquiry into whether or not there is something usefully labeled as "nonprofitness." This inquiry is part of a larger theoretical endeavor which aims to discover what the differences are between public and private institutions or activities -- if there is "publicness" or "privateness."

One of my theoretical aims in this paper has been to cast doubt as to whether nonprofit organizations (or by implication, government) are a residual category of social organization. Instead, I have tried to argue that logically and historically the market are not prior -- that "nonprofitness" or "publicness" is not simply what "privateness" cannot accomplish. By making the argument that macro-political factors influence intersectoral and intrasectoral behavior, I am making claims about what kind of factors are important in the analysis of the political economy -- I am arguing for the necessity of bringing the state back in. To go even further, by arguing for the importance of macro-political factors I am suggesting that politics and government may be prior or at least of comparable importance in shaping the relationships between the various sectors.

NOTES

1. Cash cows represent those lines of business which are central sources of cash for a conventional business firm. Because of their extremely strong competitive position in a declining market, cash cows generate more cash than they can prudently reinvest in themselves. They therefore represent a large source of cash that can be used for development of other businesses within the firm. Businesses "milk" cash cows for their cash (Hax and Majluf 1983).

When used in the world of nonprofits, the term has a more inexact usage (and wistful connotation): cash cows are businesses that yield funds that can subsidize money-losing activities that a nonprofit organization wishes to maintain or pursue.

2. By charities I mean nonprofit organizations that are (i) donatively financed, (ii) provide free or below market cost services and (iii) serve the disadvantaged.

3. This is the nomenclature that the IRS uses.

4. I describe two models developed by James in this paper. The first one, outlined in this section deals with the behavior of nonprofit organizations. The second, described in the following section focuses more on the role of nonprofits and their relationship to government and the market. There is some evolution in James's thinking which I discuss in the context of her second model.

5. In addition to the problem of how economic models treat redistribution, there are several other limitations of this form of analysis germane to the study of nonprofits including the fact that theories that account for the existence of nonprofits on the basis of market failure confound history; economic theories of institutional change frequently misuse notions of natural selection; and economic theories of cross-subsidization lack well developed accounts of second best solutions.

6. Salamon (1986, 5) notes less than one-third of the nonprofit agencies surveyed in the Urban Institute's study of the nonprofit sector indicated that they focused on serving a low income or poor clientele.

7. According to Skocpol (Evans, Rueschemeyer and Skocpol 1985, 21), Alexis de Tocqueville applied this approach in his works, The Old Regime and The French Revolution and Democracy in America.

8. Public goods are nonrival -- their consumption does not use them up -- and nonexclusive -- if they are provided to one consumer it is impossible to exclude others from consumption.

9. That is, lack of donative support in terms of proportionate shares of nonprofit revenue. For more detail on this see the section on privatization below.

10. The Philippines were an American colony at the time.

11. Subchapter S of the Internal Revenue Code allows corporations to exempt themselves from the corporate income tax if they meet certain criteria. Election of this status allows the corporations to avoid double taxation by distributing profits to shareholders without facing corporate level taxation. The profits are treated as personal income and taxed at the appropriate and generally lower individual rate (Wellford and Gallagher 1985, 11).

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WORKING DRAFT

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THE USE OF TAXABLE SUBSIDIARY CORPORATIONS BY PUBLIC CHARITIES: A TAX POLICY ISSUE FOR 1988

by

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Disputes concerning the commercial activities of exempt organizations date to the beginning of the income tax. Such disputes have continued throughout the evolution of the tax laws. As a result of these disputes, Congress has twice focused upon exempt organizations' commercial activities and charges of "unfair competition", once in 1950 and again in 1969. Despite the years of controversy, Congress' efforts, and numerous court decisions, it now seems likely that this issue will once again be scrutinized in 1988.[1] One recurrent aspect of the debate has been the utilization of taxable subsidiary corporations by exempt organizations. This subject is ripe for policy review in 1988 as the use of taxable subsidiaries has increased dramatically during the 1980s.[2] This paper will trace the evolution of the use of taxable subsidiaries, identify the reasons for their proliferation, and examine the policy ramifications of this development.

THE EARLY YEARS - THE DEBATE BEGINS

In 1913, the year in which the sixteenth amendment to the Constitution was ratified giving Congress the "power to lay and collect taxes on income..," a dispute arose between the Insular Collector of Internal Revenue of the Philippine Islands and a Philippine religious corporation over the commercial activities of that corporation.[3] The corporation derived its income from interest, rents, and dividends as well as from the sale of wines, chocolates, and other articles purchased and supplied for use in its churches and schools. The tax collector took the position that the corporation was not "operated exclusively" for religious purposes, but rather was operated, in part, for commercial purposes in that it used its properties to produce income, and traded in wines, chocolate, and other articles. This dispute was resolved in the organization's favor 11 years later. In Trinidad v. Sagrada Orden de Predicadores, the Supreme Court enunciated the "destination of income test," and held that the destination of the income - not its source - was the ultimate test of the right of exemption.[4]

During the next two decades the Internal Revenue Service (Service) was involved in similar disputes with charitable organizations that engaged in transparently profit-making activities. In one of the most celebrated cases, a corporation engaged in the manufacture and sale of macaroni was acquired and merged into a corporation organized to benefit the School of Law of New York University. The Service's assertion that this entity was neither organized nor operated exclusively for a charitable purpose was again thwarted by the destination of income test.[5] By the time the Third Circuit Court of Appeals rendered its opinion in that case, however, the law had been changed. Congress had already reacted to complaints that exempt organizations were engaged in profitable business activities in competition with taxable entities:

> .... the involvement of educational institutions

> in the field of banking, real-estate, commerce, and industry goes merrily on. Universities own haberdasheries, citrus groves, movies, cattle ranches, the Encyclopedia Brittanica (owned by the University of Chicago), and a large variety of other enterprises. The University of Wisconsin controls patent pools and collects royalties. Universities and colleges, together with foundations, have an annual income from their business activities of well over a half billion dollars annually. Were this income not tax-exempt, they would pay $173,000,000 in Federal Taxes annually.[6]

THE REVENUE ACT OF 1950 - THE DEBATE CONTINUES

The Revenue Act of 1950 devised a scheme to deal with the issue of unfair competition between taxable and exempt entities. The first part of the scheme was the enactment of the "feeder" provisions of section 502 of the Internal Revenue Code to overturn the destination of income test (feeders are business organizations that "feed" income to a tax exempt organization). Section 502(a) provides that an organization "operated for the primary purpose of carrying on a trade or business for profit shall not be exempt from taxation under section 501 on the ground that all of its profits are payable to one or more organizations exempt from taxation under section 501."[7] Congress noted that "such an organization is not itself carrying out an exempt purpose. Moreover, it is obviously in direct competition with other taxable businesses."[8]

The second part of the scheme to deal with the issue of unfair competition was the imposition of the regular corporate income tax to active business income which arises from activities which are "unrelated" to an organization's tax exempt purposes. This new "unrelated business income tax" was directed at unfair competition conducted by charitable organizations, labor organizations, and business leagues:

> The problem at which the tax on unrelated business income is directed is primarily that of unfair competition. The tax-free status of section [501] organizations enables them to use their profits tax-free to expand operations, while their competitors can expand only with the profits remaining after taxes. Also, a number of examples have arisen where these organizations have, in effect, used their tax exemptions to buy an ordinary business. That is, they have acquired the business with little or no investment on their own part and paid for it in installments out of subsequent earnings - a procedure which usually could not be followed if the business were taxable.
>
> In neither the House bill nor your committee's bill does this provision deny the exemption where the

> organizations are carrying on unrelated active business enterprises, nor require that they dispose of such businesses. Both provisions merely impose the same tax on income derived from an unrelated trade or business as is borne by their competitors.[9]

In devising this scheme to deal with unfair competition, Congress was specifically concerned with "active" business income. As such, it excluded from taxation the types of income that had traditionally been considered "passive" in nature, i.e., dividends, interest, royalties, and rents.[10] It soon became clear, however, that transactions could be structured to utilize these exclusions in conjunction with subsidiary corporations to avoid the unrelated business income tax.

Within months of the Revenue Act of 1950, for example, the Amon Carter Foundation formed a wholly-owned subsidiary corporation and transferred to it certain oil and gas leases and related machinery. It was apparent that the new unrelated business income tax rules would subject the Foundation to taxation if it operated the business. Moreover, the destination of income test was no longer available to shield the subsidiary from taxation. Accordingly, the business operation was structured so that the new taxable subsidiary corporation operated the business, and paid "income" on the oil and gas properties to the Foundation in the form of overriding royalties. The Foundation claimed an exclusion from the unrelated business income tax rules on the basis of the "passive" nature of the royalty income. The Service objected, but was unsuccessful in its assertion that, in substance, the subsidiary corporation had no separate existence.[11]

In a similar case the Robert A. Welch Foundation transferred a taxable "working interest" in oil and gas properties to its controlled taxable subsidiary corporations and subsequently reported income from these properties as nontaxable royalties. The Service asserted unsuccessfully in the Fifth Circuit Court of Appeals that the Foundation's income should be characterized, in substance, as a taxable "working interest."[12] The Service subsequently announced in a 1969 revenue ruling that it would not follow the Fifth Circuit's opinion.[13]

THE TAX REFORM ACT OF 1969 - THE DEBATE CONTINUES

By the time the Service's 1969 revenue ruling was published, Congress was again reacting to complaints of unfair competition between exempt and taxable entities. In this context there were two basic concerns. The first was the extensive involvement of private foundations - privately supported charitable organizations - in the business sector. Congress feared that charitable concerns had become secondary to business concerns. The Senate Finance Committee cited an example of one foundation which was found to control eighteen operating businesses, including a ten million dollar newspaper, the largest radio station in the state, a twenty million dollar insurance company, a lumber company, several banks, three large hotels, a garage and a number of office buildings.[14] Congress reacted in the Tax Reform Act of 1969 by imposing severe limitations on the ability of private foundations to maintain holdings in business enterprises:

> Those who wished to use a foundation's stock holdings to acquire or retain business control in some cases were relatively unconcerned about producing income to be used by the foundation for charitable purposes. In fact, they might have become so interested in making a success of the business, or in meeting competition, that most of their attention and interest was devoted to this with the result that what was supposed to be their function, that of carrying on charitable, educational, etc. activities was neglected. Even when such a foundation attains a degree of independence from its major donor, there is a temptation for its managers to divert their interest to the maintenance and improvement of the business and away from their charitable duties. Where the charitable ownership predominates, the business may be run in a way which unfairly competes with other businesses whose owners must pay taxes on the income that they derive from the businesses. To deal with these problems, Congress concluded it is desirable to limit the extent to which a business may be controlled by a private foundation.[15]

Congress' second basic concern was that many of the other exempt organizations that were excepted from the unrelated business income rules (including churches) were engaging, or were apt to engage in, unrelated business. Congress responded by expanding the coverage of the unrelated business income tax to virtually all exempt organizations. In addition, there were changes limiting the types of income excepted from the unrelated provisions. One such provision was designed to prevent parent-subsidiary corporate transactions from escaping taxation through the use of sophisticated interest, rents, annuity, and royalty schemes. Specifically, section 512(b)(13) was amended to provide a "controlled organization test," i.e., a test providing that in those situations where a tax exempt organization owns more than 80 percent of a taxable subsidiary, the interests, annuities, royalties, and rents received by it from the subsidiary are to be treated as unrelated business income and are subject to tax in the hands of the exempt organization. This, of course, was a legislative response to those earlier cases where exempt organizations caused the profits of their controlled corporations to be passed on to them in the passive form, thereby avoiding the tax on the subsidiaries' income:

> In certain cases exempt organizations do not engage in business directly but do so through nominally

> taxable subsidiary corporations. In many such instances the subsidiary corporations pay interest, rents or royalties to the exempt parent in sufficient amount to eliminate their entire income, which interest, rents, and royalties are not taxed to the parent even though they may be derived from an active business.
>
> This problem is remedied under the bill by removing the exemption from the unrelated business tax for passive income if it is in the form of interest, rents, and royalties received from controlled corporations.[16]

This statutory change did not put the practice to rest. Indeed, two years after the 1969 amendment the Service assessed taxes against the Mabee Foundation. In that instance the Mabee Petroleum Corporation - a wholly-owned taxable subsidiary corporation of the Mabee Foundation - engaged in the production and sale of oil and gas through ownership of oil and gas leases. The Foundation, as holder of the overriding royalty interests, received payments directly from the oil purchasers rather than indirectly through its subsidiary, which would have been the customary method of receiving such payments. The Foundation, while admitting that the subsidiary was a "controlled organization," argued that the overriding royalties should be excluded from unrelated business taxable income because the income was not "derived from" the subsidiary within the purview of section 512(b)(13) but rather from the oil purchasers directly. Neither the trial nor the appellate courts found this argument convincing. Indeed, the Tenth Circuit Court of Appeals described the method of payment as a "scheme...within the manipulations which Congress sought to tax:"

> It is of no consequence that Foundation and Petroleum had arranged for Foundation to receive the money directly rather than through Petroleum. Petroleum produces and markets the gas and oil to generate the production income upon which Foundation's overriding royalty income is based. Taxation does not depend on the mechanical formality of whether the overriding royalty income was paid through the controlled organization generating the income or directly to the charitable recipient. It appears clear beyond peradventure that Congress intended to tax a charitable organization's receipt of customary "royalties" from a "controlled organization."[17]

THE 1980s - EXEMPT ORGANIZATIONS CHANGE - THE DEBATE INTENSIFIES

The interest of exempt organizations in utilizing taxable subsidiary corporations increased significantly in the past decade. A decline in traditional funding sources and an increase in demand for services forced many exempt organizations into the commercial arena.[18] The Urban Institute's Nonprofit Sector

Project, for example, found that federal support for the nonprofit sector declined an estimated $4.5 billion between 1980 and 1984, and that this decline was offset in large part by commercial sources of income.[19]

To survive in a dramatically changing economy, many section 501(c)(3) organizations began to revise their corporate structures. The increased use of taxable subsidiary corporations was a part of this strategy. For example, the Service issued 593 private letter rulings to section 501(c)(3) organizations that operated in tandem with taxable subsidiary corporations between 1977 and 1986. In comparison, there were only 8 equivalent rulings issued in the previous ten year period.[20]

This change was most notable in the health care sector as 435 of the 593 rulings involved health care organizations.[21] Nonprofit community hospitals particularly felt the brunt of a changing economy. Government, business, and third-party payors sought to control health care costs that had escalated wildly in past years of high inflation and double digit interest rates. In addition, the federal government moved away from a cost reimbursement system under the Medicare program to a prospective payment system based on pre-set prices. As this financial reimbursement system was changing, nonprofit hospitals were faced with competition for patients and doctors from chains of aggressive for-profit corporations. In order to survive in a changing, heavily regulated, and intensely competitive environment, nonprofit hospitals began to diversify by reorganizing into multi-entity structures.[22] In most instances, a taxable subsidiary corporation was included in the new system.

Subsidiary corporations continue to be utilized in these systems to structure transactions so that income flowing between the corporations can be characterized as nontaxable passive income. In the early 1980s, for example, the District Director in Detroit sought advice from the IRS' National Office about a parent-subsidiary corporate transaction in a hospital system that sought to escape the unrelated business income tax through the use of a sophisticated rent arrangement similar to the one used in the Mabee Foundation case. The transaction involved a tax exempt parent holding company that controlled two wholly-owned subsidiaries: a tax-exempt hospital and a for-profit pharmacy and optical shop. The hospital leased space in its facility to the for-profit pharmacy and optical shop. Rental payments from the for-profit entity were made to the tax exempt hospital and not to the parent corporation. As the hospital did not control the for-profit subsidiary, the parent corporation claimed that the rent payments to the hospital were not subject to section 512(b)(13) or the unrelated business income tax. As in the Mabee Foundation case, this scheme was an attempt to structure the transaction so that typically "passive" income payments are received from third parties rather than from the exempt organization's controlled corporation. It was the opinion of IRS' Office of Chief Counsel, however, that the interposition of a wholly-owned entity between the exempt controlling organization and the wholly-owned source of the payments may be disregarded for purposes of applying the unrelated business income tax. Accordingly, rent payments to the hospital were deemed subject to section 512(b)(13) and the unrelated business income tax.[23]

1987 -CONGRESSIONAL HEARINGS

On September 12, 1986, the House Ways and Means Committee announced a hearing to review the federal tax treatment of commercial and other income-producing activities of tax exempt organizations and related entities.[24] Five days of hearings were held in June of 1987. The Deputy Assistant Secretary (Tax Policy) of the Treasury Department presented the government's policy views on the appropriate tax treatment of income-producing activities of exempt organizations and related entities.[25] This testimony, which was comprehensive in scope, made two recommendations for revision of the tax laws that pertain to the use of taxable subsidiary corporations.

The first recommendation was to revise the controlled organization test of section 512(b)(13). Treasury noted that an exempt organization could own 100 percent of the voting stock of a subsidiary, 99 percent of the total value of a subsidiary, but only 79 percent of a single class of nonvoting stock, and not technically fall within the definition of a controlled organization. Treasury's recommendation was that the definition of a controlled organization should be changed to include an organization in which the parent exempt organization has more than a 50 percent interest, measured by either voting power or value. In addition, Treasury suggested that application of the ownership attribution rules be enacted so that a subsidiary controlled by an affiliate of an exempt organization would be covered.

Treasury also suggested that consideration be given to aggregating the activities of an exempt organization and its subsidiaries. Under present law, a section 501(c)(3) organization can engage in a business as a substantial part of its activities so long as the operation of the business is in furtherance of its exempt purpose and it is not organized or operated for the "primary purpose" of carrying on an unrelated business. Treasury recommended that, in appropriate cases, the activities of an exempt parent and its subsidiaries should be aggregated to test for the exempt organization's primary purpose (especially where management of the subsidiary is fully integrated with that of its parent).

These recommendations were subsequently endorsed in an October 15, 1987, letter to the Chairman of the House Ways and Means Subcommittee on Oversight from four Republican members of that Subcommittee.[26] As such, they are likely to receive serious consideration by the full Ways and Means Committee in 1988.

1988 AND BEYOND - WILL HISTORY BE REPEATED?

In 1950, Congress attempted to create rules that would prevent exempt organizations and their subsidiaries from competing unfairly with taxable businesses. Nineteen years later, in 1969, Congress recognized that the problem had not been solved by its 1950 legislation and created additional rules to restrict exempt organizations' use of taxable subsidiaries. Now, once again nineteen years later, Congress may find it necessary to enact yet more legislation attempting to prevent exempt organizations from using taxable subsidiaries to unfairly compete with other taxable businesses. Certainly, Congress' current concerns in this area are nearly identical to the concerns that Congress expressed in this area prior to enacting legislation in both 1950 and 1969.

Perhaps, then, the basic issue to be considered as Congress ventures into its third major review of the tax laws dealing with the issue of unfair competition, is whether perceived abuses can be dealt with through continued microscopic revisions to a very comprehensive tax law. This paper has demonstrated that exempt organizations have, over the years, utilized creative tax planning to cause the profits of their controlled corporations to be passed on to them in passive form, thereby avoiding the tax on the subsidiaries' income. Previous Congressional responses have not been successful in dealing with this situation. If history is a guide, the suggested revision to the controlled organization test of section 512(b)(13) may prove, once again, to be only a temporary obstacle to those seeking to characterize income as passive (i.e., nontaxable) in nature. Indeed, it must be questioned whether any controlled organization test will be effective with respect to the new "systems" of exempt entities. As indicated earlier, the recent explosive use of taxable subsidiary corporations has primarily been in the hospital area where the single exempt entity has spawned a system of related exempt and taxable entities. While section 512(b)(13) only applies to transactions between a parent corporation and a controlled corporation, it is questionable whether that statute, or any revision to that statute, will be effective in dealing with a potentially unlimited number of transactions that can be structured between brother-sister corporations in a system of exempt entities.

Similarly, the proposed commercial activity aggregation rules may not be effective in the hospital area. The difficulty of applying a primary activity test in the hospital area is that the gross income from hospitals is larger than that of any other type of public charity.[27] As such, hospitals will be able to aggregate a significant amount of business activity without failing a "primary purpose" test.

If perceived abuses cannot be effectively addressed through continued microscopic revisions of a very comprehensive tax law, the alternative is macro change. In looking for an effective macro change, the obvious model is the excise taxes imposed on private foundations in the Tax Reform Act of 1969. The excess business holding rules were specifically designed to deal with business involvement of privately funded section 501(c)(3) organizations.[28]

There are current indications that an extension of these rules to public charities may be appropriate. For example, one concern expressed in 1969, that charitable interests of private foundations had become secondary to business interests, is closely parallel to similar concerns expressed about public charities today. One of the former Directors of the Urban Institute, for example, offered the following opinion on the findings of the Institute's Nonprofit Sector Project:

> As government support declines, private charity fails to fill the gap, and organizations turn increasingly towards commercial sources of income instead, the sector's willingness and ability to serve those in greatest need may decline, undermining the sector's **raison d'etre** in the process.[29]

In addition, the opinion of one noted exempt organizations commentator in 1984 suggests that the point for macro change has already been reached:

> [3] Subsidiaries and Subordinates....
> So for now, the quietly efficient, multi-tiered charitable enterprise, selling its related and unrelated goods, service or facilities, to charitable classes of the public, to customers generally and to governmental units, does not see the Service as a threat to its integrity, but merely as an unruly, but manageable, partner. Congress seems unlikely to act on its own initiative, the Treasury Department seems unwilling to spend its meager resources in yet another study, and the public does not seem to sense that the magnitude threatens its peace and good order. The business community seems to be the only remaining interested party; and since it appears that the economy is sufficiently expansive to be hospitable to all newcomers, regardless of cloak or mantle, that community seems content to absorb or accommodate its charitable competitors.[30]

It is critical, however, that this suggestion be scrutinized with extreme caution. To begin with, there is a lack of data about the extent of commercial activity of exempt organizations.[31] Moreover, while it is clear that federal support for the exempt sector has declined dramatically in recent years, and while it is also clear that sophisticated exempt organizations have entered the commercial arena in response to this decline, it is not known whether the priority of these organizations is the bottom line or the provision of services. Historically, the major initiatives in addressing significant issues of medical care, housing, education and employment have emanated from the exempt sector. If the economic base of today's exempt organization is dramatically slashed without considering ways to continue these contributions, major difficulties may arise in the provision of social services in the future, particularly during a recession or when the business economics of the marketplace are otherwise unfavorable.

1. Rep. Rostenkowski Announces 1988 Agenda for Ways-Means Oversight Subcommittee, Daily Tax Rep. (BNA) No. 243, p. G-1 (December 21, 1987).

2. See, infra, ns. 20-21 and accompanying text.

3. At that time the Philippine Islands were a territory of the United States.

4. 263 US 578 (1924).

5. C.F. Mueller Co. v. Commissioner, 190 F2d 120 (1951).

6. Cong. Rec., Vol 96, Part 7, pp 9273-9274.

7. IRC sec. 502(a) (1986). Statutory references in this paper are to the Internal Revenue Code of 1986, as amended.

8. HR Rep No 2319, 81st Cong, 2d Sess at 41 (1950). S Rep No 2375, 81st Cong, 2d Sess at 35 (1950).

9. S Rep No 2375, 81st Cong, 2d Sess at 27 (1950).

10. IRC sec. 512(b)(1) through 512(b)(3).

11. Amon Carter Foundation v. United States, 58-1 USTC (CCH) 9342 (ND Tex 1958).

12. United States v. Robert A. Welch Foundation, 334 F2d 774 (5th Cir 1964).

13. Rev Rul 69-162, 1969-1 CB 158.

14. S Rep No 91-552, 91st Cong 2d Sess at 39 (1969).

15. Joint Committee on Internal Revenue Taxation, General Explanation of the Tax Reform Act of 1969, 91st Cong 2d Sess at 41 (1970).

16. H R Rep No 91-413 (Part 1), 91st Cong, 1st Sess at 49 (1969); S Rep No 91-552, 1st Sess at 73 (1969).

17. The J.E. and L.E. Mabee Foundation v. United States, 533 F.2d 521 at 524 (10th Cir. 1976).

18. McGovern, "The Changing Character of Exempt Organizations," 19 Phil Monthly 19 (1986).

19. Salomon, "The Results are Coming In," 25 Found. News 16, 17 (1984).

20. These statistics are based upon an automated search of a private ruling letter data base.

21. Id.

22. McGovern, "Restructured Nonprofit Hospitals," 35 Tax Notes 405 (1987, No.4).

23. GCM 38878, July 16, 1982.

24. Committee on Ways and Means, U.S. House of Representatives, Press Release #25, (September 12, 1986).

25. Statement of Hon. O. Donaldson Chapoton, Depty Asst Secy (Tax Policy), Dept of the Treas., Before the Subcommittee on Oversight of the Committee on Ways and Means.

26. Initial Recommendations by House Ways and Means Oversight Subcommittee Republicans on Unrelated Business Income of Tax-Exempt Organizations, dated October 15, 1987, Daily Tax Rep. (BNA) No. 206, at J-1 (October 27, 1987).

27. IRS Statistics of Income Bulletin, Winter 1985-86, p. 26.

28. IRC sec 4943.

29. Id. at 23.

30. Lehrfeld, "Dealing with Investors and Other Methods of Generating Income: Tax Aspects of Revenue Producing Activities," 42 Inst. of Fed. Tax'n 26-1 (1984).

31. Despite a comprehensive search, the General Accounting Office could not find such data. GAO examined the IRS' Statistics of Income and Exempt Organizations Business Master File data bases. In addition, GAO examined studies by the Bureau of Census in 1977 and 1982, the Urban Institute in 1982, the Partners for Livable Places and the Rockefeller Brothers Fund in 1982, the Independent Sector in 1984, the Small Business Administration in 1984, and the National Assembly of Voluntary Health and Welfare Organizations in 1985.

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MORE GOVERNMENT SUPPORT FOR NONPROFITS: IS IT WORTH THE COST?

by

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Prepared for the 1988 Spring Research Forum
"Looking Forward to the Year 2000:
Public Policy and Philanthropy"

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More Government Support for Nonprofits:
Is It Worth the Cost?

By Jack Moskowitz - Vice President
Federal Government Relations

United Way of America

The Private NonProfit Sector faces a future dilemma in deciding on its relationship with Federal, State and Local governments. That is: (1) does it recognize the extent of dependence on government funding of its activities; and (2) does it realize that the amount of private funds are limited, and consequently any substantial growth in services will require more government funds?

The facts are clear: In their study, The Federal Budget and NonProfit Sector (Washington: The Urban Institute Press, 1982), Lester M. Salamon and Alan J. Abramson found that in 1980 "Private philanthropic giving totalled $48.7 billion. Of this total, $22.2 billion went to churches, synagogues, mosques, and other religious congregations mostly for sacramental religious purposes. That left $26.5 billion for other types of nonprofit organizations. In that same year these other types of nonprofit organizations had a total expenditure of approximately $116 billion dollars. Of this sum the Federal Government contributed $40 billion dollars."

Salamon and Abramson's findings are supported by a 1986 United Way of America survey (1986 Local United Way Fund Distribution Results By agency, By Program, United Way of America Research Division). The 1986 United Way of America study showed that over 41% of United Way agencies' income came from government -- almost twice the amount that came from the next largest source, fees and dues (21.9%), and 4 times the amount from the agencies' own fund raising efforts (10.3%). United Ways account for only 13.3% for their funding. Many of these United Way agencies that provide services and are advocates for the poor, minorities, under privileged and disabled, receive more than half of their funding from government, i.e., day care centers 52%, drug abuse agencies 64%, legal aide agencies receive 59%, mental health agencies 65%, social welfare planning organizations 71%, retarded citizens 68%, settlement housing neighborhood centers 51%, urban league affiliates 56%, and women crisis agencies 51%. One can draw only one conclusion: without substantial government support, many essential services for those in need would suffer; even under the most optimistic appraisal of private fundraising efforts, there is no way that private sector could fully replace government support. Even such efforts as United Ways Second Century Initiative to double resources in 5 years would fall short.

As Lester Salamon points out, "The result is an elaborate system of "government-nonprofit partnership" that takes a variety of different forms and spans virtually every program area. In part, nonprofit organizations deliver a larger share of government funded human services -- than do government agencies themselves."

Yet, if one listens to most spokespersons for the nonprofits, one would never guess the pervasiveness of government in the sectors' activities. It is easy to understand the reluctance to trumpet the amount of tax dollars in the system. There is the long history of charities extolling their accomplishments and the belief in the importance of their ability to function efficiently and independently. Also, fundraising drives obviously are not going to be helped by advertising that a major funder, in many cases, is Uncle Sam. The accomplishments and promotion of an organization take place in a fundraising environment where the natural tendency would be to highlight the private effort and down play government's role. So the growth and success of this effective partnership has been the secret of the agency professionals, their program planners and those who lobby to maintain or increase funding in Congress, state capitals, county buildings and City Halls.

Unfortunately, the years of suppressing the government funding role and touting private sector accomplishments created an erroneous impression that given a chance the private sector could maintain a high level of services alone. The consequences were a climate where it was politically easy to make large cuts in federal support for a vast array of programs administered by local nonprofit agencies. Salamon's study reports that the inflation - adjusted value of federal support to private nonprofit organizations, outside of Medicare and Medicard, was 28 percent lower in 1986 than it had been in 1980.

An example is the cuts made in the Title XX Social Service Block Grant, the major federal source of funds for a wide range of essential social services such as day care, counseling, home maker and chore services for older adults, protective and health services, home delivered meals and community based services for the disabled. All of these services are provided by nonprofit agencies. The 1981 Omnibus Budget Reconciliation Act, the key budget cutting vehicle for the Reagan Administration, cut this program 20% and the program had been frozen at 1984 levels until a modest increase was enacted for 1988.

Other examples where charitable entities are the prime service providers are the sheltering and feeding of the homeless and housing for the elderly. The purpose of this paper is not to document the need for more services. The need is evident. Obviously those needs will not be fully met without more tax dollars.

The questions for nonprofits are: are they willing to openly acknowledge that although they are in an unique position to deliver quality services, greater government funding will be necessary in order to expand these services? Are they willing to openly wage a public relations and political battle for increased government funds? An affirmative answer cannot be taken lightly. The political implications with their possible back lash are great. Any attempts for increased funding are sure to be controversial and have some negative impact on fundraising and volunteer involvement.

The general non-controversial nature of many charities will have to change, a key departure for organizations who rely on broad support for their endeavors. More tax dollars also means more regulation and supervision by government. Recent Office of Management and Budget attempts to require more stringent accounting of nonprofit lobbying activities is a good example.

The kind of campaign that will be needed is one similar to the one for the nonitemizer charitable deduction. Advocating for increased charitable tax incentives, however, had almost unanimous support. Unanimity is sure to be a difficult attainment for budget battles. But, where there is strong public support and the need is evident, consensus is possible. United Way of America Board of Governors, for example, supports increased funding for the Social Services Block Grant and elements of welfare reform that would include transitional health care benefits, training and day care for recipients who take jobs and welfare eligibility for two parent families.

If the sector is willing to burden itself with the problems, expanded government private sector partnerships could provide greater and more innovative services targeted to those in need. This willingness by the private sector is the question for the '90s.

The Emergency Food and Shelter Program is a case study of the potential dramatic and unique possibilities of government nonprofit partnerships to help those in need plus the problems this partnership brings.

Since March 1983 United Way of America and five other national charitable organizations -- American Red Cross, Council of Jewish Federations, The Salvation Army, Catholic Charities, and the National Council of Churches, have been partners with the Federal Government in an emergency program to deliver food and shelter services.

The program produced results. Needy people received food and shelter. The government designed a distribution system and appropriated money that reached the intended beneficiaries. A new system and partnership with private charities was tested. It succeeded. Clearly, Congress thinks so, since each year thereafter it has appropriated money for the program. In the 1987 session the program was authorized at $125 million dollars a year.

With hindsight it is easy to see how this unprecedented partnership program came into existence. During the winter of 1982 Congress was looking for ways to deal with the growing problems of the unemployed. The employment rate at the time was over 10%. For political as well as humanitarian reasons members of Congress were seeking ways to deal with the increasing needs of a larger and larger number of people. The media was reporting thousands of people applying for every job opening. They filed stories from every part of America about people that had never been without a pay check, who suddenly had to deal with finding services that could help them keep their homes, feed their children and pay their medical bills when insurance ran out. At the same time President Reagan was sounding the theme of voluntarism, of Americans helping each other, as a way to solve social problems. The Federal Government should not be the answer to all needs, he said. Instead there should be a return to the time when people look to one another for help.

In March 1983 a combination of these factors led to Congress creating a program, federally funded, that would be administered by charitable organizations to help alleviate emergency demands for food and shelter. The idea of Federal funds being handed over for private distributions was a new one. It had only been tried once before in 1980 when the government collected a windfall profits tax from energy companies because they had over-charged American consumers. The Carter Administration decided to give this money to private charities to use for people who could not pay their utility bills. The sum was small and quickly distributed. Congressional Institutional memory did not forget this successful experience, so that in the fall and winter of 1982 when the House Democratic leadership was putting together a jobs bill that also included other social service programs, the leadership, sensitive to the growing problem of hunger and homelessness and remembering the old energy program returned to this delivery system. However, this new program involved a much larger amount of money, and was concerned with the mechanism by which an immediate need could be met, not with the best way of carrying out a legal obligation.

The final bill passed in March 1983 included a provision for $100 million dollars for emergency food and shelter to be distributed into two programs: 1) $50 million to a "State program", an often used service delivery approach, in which the funds would go to the states and the states would design distribution systems, and 2) the balance to a "Nonprofit Program", a new design for delivering federal funds, in that the federal government was putting up the money but private and nonprofit organizations would decide how to spend it.

This surrender of control prompted a certain amount of concern that the funds would not reach their intended goal quickly and equitably. Congress fortuitously decided to include a federal representative, the Federal Emergency Management Agency, on the national board. FEMA convened and chaired the national board made up itself and the United Way of America, the American Red Cross, Salvation Army, National Conference of Catholic Charities, National Council of Churches, and the Council of Jewish Welfare Federations. The national organizations had worked with Congress in

designing this delivery system and had promised that their expertise and resources would result in a speedy and fair delivery of the federal funds to people in need. FEMA was selected as the federal agency involved because of its experience with dealing with emergencies, and this situation was deemed an emergency. FEMA, however, had never been involved in a program like this before, and the nonprofit organizations had never jointly administered a program of this magnitude. No one was quite sure then what would happen at the first meeting of the national board.

Congress had purposely left it to the board to decide how to distribute the funds, largely because the political pressures would be so strong if Congress itself allocated the funds. It is to the credit of all members of that board that they had the flexibility and the vision to realize that they could all help each other in organizing the program. The strength of the committee process is that shared resources are greater than that of any one individual. The weakness of the process is the tendency to bog down in detail. Perhaps because of the deadline the board had, and perhaps because of its particular mission, the board functioned close to ideally. It became immediately clear to FEMA that the charitable organizations did have valuable expertise in the details of delivering human services. It became clear to the charitable organizations that FEMA was invaluable in helping anticipate the problems of administering a federal program.

According to the legislation, by April 23, 1983, FEMA was to release the $50 million to the board, specifically to United Way of America which has been chosen as the board's fiscal agent and secretariat. The customary pattern for federal grants is that the funds are released in a letter of credit which the recipient can draw down on as the need arises. This

process enabled the federal government to continue to receive interest on the unspent part of the grant.

Because of the character of this grant, the charitable organizations were able to persuade FEMA to take an unusual step. FEMA released the full $50 million, in two installments, to United Way of America so that the interest raised meant that, in the Nonprofit Program, the final amount distributed for emergency food and shelter was $50,776,532.

Congressional belief that the private charities unfettered by political considerations would be better able to allocate on needs basis proved to be true. Senators and Congressman from the high unemployment midwestern states in an attempt to ensure that their states would get a fair share of the appropriations for jobs, included an allocation formula in the jobs portion of the bill weighted towards their states. Subsequent examination by Senator Levin (D-MI) and Senator Specter (R-PA) showed that the formula developed by the National Emergency Food and Shelter Board was much more targeted than the congressional attempt.

Those communities receiving funds set up parallel local boards, made up of local government officials, nonprofit organizations and others in the community familiar with Emergency Food and Shelter distribution. These local boards were given two short weeks in which to plan their allocations to the agencies in their communities. The money was appropriated in March and by the end of May the first checks were rolling out directly to the agencies providing additional food and shelter. By the end of September 80% of the nonprofit funding had actually been spent.

The state program however, was not that successful, and only distributed a small amount of its funds by the end of the fiscal year. Therefore in the next year's appropriations Congress dropped the state program, and provided only for the nonprofit program.

The Emergency Food and Shelter Program by no means was meant to solve the problem of the homeless; it was meant to meet an emergency situation. Although it may not have helped everyone in need, the people it did serve were in need. Besides the actual feeding and sheltering of the needy the program had unexpected side benefits. The effort of local boards of nonprofit organizations and government representatives resulted in an unique focus on a community problem, and a building of alliances and links that have already met more responsible consideration of other community problems.

In one city, for example, the local board was asked to continue to serve by the local government in order to deal with the other community needs. Everyone involved in the program learned that the Federal Government can play a role in addressing real community problems in a successful and timely way. The actual meals and nights' lodging provided by the funds are the purpose and goal of the program, but may in the long run have been one of the most transitory benefits of the program. More important are the alliances and relationships built up among charitable organizations, and the localities that received funding, and also, between those organizations and local elected officials.

Members of the national board, too, received a valuable education on how private and public organizations could work together. The experience of a board made up of national and charitable organizations and representatives of the Federal Government proved to be effective at solving problems.

Of course the program was not without problems. The greatest single problem is that the small amounts appropriated in this program cannot solve hunger and homelessness in America. What the Nonprofit Sector can do is limited. Providing for basic welfare needs will still be the province of government. Foodstamps, welfare payments, etc. are best administered by government.

In the beginning, Congress and the charities viewed the program as a temporary experiment, and all agreed to a low (2%) allowance for administration costs (most other programs have costs of 10% or higher). In fact, at the outset United Way of America, acting as fiscal agent for the Board, waived considerable costs as did many provider agencies. As the program went on, the low cost allowance caused severe strains on agency personnel and resources. A low key, almost embarrassed lobbying effort got authorizing legislation to raise the cost cap to 5% for 1988. However, the appropriation only allowed 3 1/2%. The agencies involved were reluctant to press for more costs though they were needed. Such lobbying seemed unseemly.

Finally, the administering and distribution of government funds raised serious legal questions as to the status of the national and local boards. The Justice Department is of the opinion that this legislation presents serious constitutional problems under the appointments and establishment clauses of the first amendment to the constitution. They believe that the board is vested with a significant governmental duty, and therefore must be officers of the United States, and that potentially because of the involvement of religious groups there may be a degree of government involvement with religion.

The president in signing appropriations for the Emergency Food and Shelter Program noting this problem has said, "in order to void this constitutional infirmity I direct the director of FEMA to construe this provision as granting him complete discretionary authority to determine who should be appointed to the national board." So far no actual problem has occurred. The director of FEMA has appointed the existing representatives from the national agencies to the board and they have operated as in the past. However, the board members were required to take an oath and file conflict of interest statements as any other Federal employee -- a requirement that has rightfully made the participants uncomfortable and could portend more problems in the future. Under this interpretation, the Director of FEMA could change or enlarge the Board and impose other restrictions that could be onerous to the agencies. Also, these requirements have imperceptibly altered the relationship between FEMA and the charitable members of the Board.

The nonprofit government partnership structure of the Emergency Food and Shelter Program is a model for success. There is no practical reason why such a structure could not be used to provide summer camp experiences for underprivileged youth, job training and literacy programs. We know it can work. If the nonprofit sector wishes to make the leap and promote more experimental program partnerships with government, they will have to face that such participation may run against the grain of long held philosophies and infringe on the sector's independence. The sector must recognize that a visible intense lobbying effort will be required to maintain and keep the programs going.

When the Emergency Food and Shelter program was originally proposed, many in the nonprofit sector movement were concerned that the program would take on the look of a bureaucratic public welfare agency. Much of this has come true. The program is now highly organized, has a staff of it own, and functions much like any other bureaucratic organization. Lobbying will continue for funding. A low key lobbying effort has kept this program going though the needs of the homeless and the hungry are ever increasing. An allout effort for more funds has not been possible, I believe, because most of the charities involved in the program feel very uncomfortable seeking what they think is a government handout.

If expansion of this program is to be had, the essential constitutional questions are going to have to be dealt with and solved. Not only in this program has the question of government involvement with religion been raised, but it has been raised in other programs for the homeless, and senior citizens' housing and community meals programs. New structures may be required to ensure that there is a separation of church and state but still permit government funding of religious social service agencies who have the most experience and are major providers of services to the needy.

There is no question that the nonprofit sector contributes greatly to those without, and has the capacity to do much more if funds were available. The amount of private funds is limited. Maximum expansion and experimentation will not be realized without more federal funding.

To get additional funds, the extent of government funding of charitable programs will have to be exposed and the consequences dealt with. Going into partnership with government brings risks, responsibilities, controls, controversy and interference. It's up to the private nonprofit sector to decide if they want this challenge.

SECTION FIVE:

VALUES AND ETHICS

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FAMINE AND PHILANTHROPY: THE ETHICS AND VALUES OF INTERNATIONAL RELIEF

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Famine and Philanthropy:

The Ethics and Values of International Relief

> The news report was of famine in Ethiopia. From the first seconds it was clear that this was a horror on a monumental scale. The pictures were of people who were so shrunken by starvation that they looked like beings from another planet.... The camera wandered amongst them like a mesmerized observer, occasionally dwelling on one person so that he looked directly at me, sitting in my comfortable living room surrounded by the fripperies of modern living which we were pleased to regard as necessities....
>
> Right from the first few seconds it was clear that this was a tragedy which the world had somehow contrived not to notice until it had reached a scale which constituted an international scandal....
>
> The images played and replayed in my mind. What could I do? I could send some money. Of course I could send some money. But that didn't seem enough.... To expiate yourself truly of any complicity in this evil meant you had to give something of yourself.

This essay is a commentary on that passage from the autobiography of British rock musician Bob Geldof. Stripped to its essentials, Geldof's experience offers a model of the modern philanthropic mind at work (in my words, now, not his):

- This news affects me, personally.

- These images are unbearable.

- This terrible thing has been going on and I've been so preoccupied with myself that I didn't even know it was happening. I am comfortable and secure while these people are in agony and near death.

Two questions arise immediately: Why was the news so late in coming? Why was the response so great?

The first question is off the mark. There had in fact been news reports of an approaching African famine; the early warning system had detected the first signs as much as a year earlier (and on a fragmentary basis, as early as 1982). As relief expert Nan Burton of International Voluntary Services put it, "It isn't early warning we need: it's early attention."

The NBC executive who was in charge of the London bureau when the BBC report first appeared was Joseph Angotti. His response was professional as well as personal. He responded as Geldof (and Tom Brokaw and millions of others) had responded, but in almost the same moment made the professional decision that *this* report was different. It was more powerful, somehow. Angotti's insistence that Brokaw and his producer in New York look at the film caused them to scramble their plans for the evening news telecast and include the BBC report.

Why were these pictures different? Why did so many people respond with gifts and other offers of help?

No one seems to know. There had been other film of famine in Africa carried by NBC earlier. The photographic subjects at that time were the victims of famine and civil war in Chad. Those news reports generated not a single telephone call to NBC News. Is there a lower level of human interest in suffering in Chad than in Ethiopia? Or is the difference in response explicable only on aesthetic grounds? (Amin and Burke returned to Ethiopia in 1985 to photograph the camps a year later; those pictures -- commissioned by NBC this time -- were never used. The professional judgment was that the second film was less powerful than the first. There had been a little rain: there was some green grass in the background....)

Whatever the cause, tens of thousands of contributions flowed into the offices of private voluntary organizations all across the United States (and Canada and western Europe). The initial wave of response caught the organizations off-guard. Only four American organizations had programs in Ethiopia: within a few months there were two dozen. News coverage blossomed. *Newsday* had sent a team before the NBC story appeared, and its Pulitzer Prize winning series by Josh Friedman appeared in November. Well-known public figures began to travel to Ethiopia along with journalists: Senator Kennedy's visits to the refugee camps were covered by *People magazine*. Bob Geldof

- I can do something about it. I can give money -- but giving money isn't enough. I have to become involved.

Bob Geldof is a professional musician. His thoughts carried him along this path of reasoning (again in my summary):

- Other people are like me. We can work together. We can organize something and use our talent and skills to generate more money than any of us could give. We'll use every professional trick we know. We'll work with others who don't feel the same way we do, if we have to. We'll raise money quickly, before Christmas when people will be more generous. And we'll get the money directly to the people who need it.

- We'll give our talent and our money and we won't ask anything in return.

- We'll do this with or without permission. This is going to be our show.

- We'll feed those starving people. I will. My friends and I.

The same images that Bob Geldof watched on BBC were later carried by NBC television in the nightly news from New York. The film had been taken by an African, Muhammad Amin, working with narrator Michael Burke, both employed by VisNews on assignment from BBC. Amin had been the catalyst, and had managed to win permission from the Ethiopian government to take pictures at the refugee camp at Korem. The report had the same stunning impact in the United States it had had in England a few hours earlier. The NBC News telephone lines were jammed with calls. By the next morning there were people lined up outside the offices of international relief agencies waiting to make contributions. Geldof's personal reaction was replicated literally millions of times in the United States and Europe.

organized a recording that became an instant success, inspiring the American recording of "We Are the World" that met with similar success here.

Between October 1984 and mid-summer 1985, America and Europe were engaged with public and private efforts on a vast scale to relieve the suffering of the estimated 14 million people at risk in Ethiopia alone. Public enthusiasm overwhelmed the political obstacles: at first, the Mengistu government in Ethiopia denied there was a famine, and then blamed it on the United States. The government of Ethiopia styles itself "Marxist-Leninist," suggesting to some observers that aid of any kind would merely entrench an oppressive regime. The secessionist rebellion in Eritraea in the north was also Marxist, and the long struggle against the regime in Addis Ababa continued unabated despite the famine.

The political dimension became more intrusive when charges appeared in the Reader's Digest (from the head of the French medical relief organization Medecins sans frontieres) that relief funds and supplies were being used by the Ethiopian government in its effort to force the relocation of large numbers to camps outside the troubled areas of the north.

The position of almost all relief organizations, American and European, was the same: ignore the politics and help the people. If it was necessary to cooperate with the Ethiopian government in order to bring aid to its own starving people, then cooperation was called for. The intricate and sensitive negotiations that made the relief effort possible appear to have been facilitated by the United Nations coordinator in Addis Ababa, working closely with the director of the Ethiopian governmental relief and rehabilitation agency. (The Ethiopian administrator later defected to the United States, adding his voice to the denunciation of the Mengistu regime.)

The logistical problems of shipping the food, unloading it, reloading it onto trucks, and transporting it to refugee camps and other locations were enormous. According to assessments of relief operations, the Ethiopian government did not interfere with food distribution once it began.

Outsiders often failed to notice or simply brushed aside signs of the Ethiopian government's concern for its dignity and public image. At the very moment when the famine was entering the crisis stage, the Ethiopian government spent more than $100 million for facilities to host the meeting of the Organization of African Unity. At the very moment when news reports appeared about the desperate circumstances in the countryside, the government was trying to present itself to the world as a model of Marxist-Leninist leadership in the Third World. No government is proud of a disaster of such magnitude when its own policies might be part of the cause. In a way, Ethiopia was treated by well-meaning outsiders as unfortunates are usually treated: with little concern for the self-respect of the victim. (Compare the resentment of "friendly visitors" to the homes of the poor in 19th century England; compare the condescension shown toward those whose problems seem to be of their own making.)

International relief activity seeks to bring help directly to those in critical need of food, shelter, and medical supplies. In the wake of those first efforts follow steps toward rehabilitation: getting the people out of the camps and back to their homes. That process gradually turns into the third stage: the efforts to change conditions so that the families become self-supporting and better prepared when the next drought occurs. To move through those three stages in the midst of civil disorder and open warfare, attempting to work with a government whose own proposed solutions to its problems seem doomed to failure, is to expect more than is likely to be achieved even under less difficult conditions.

What tentative conclusions might be reached about the political dimensions of the response to the famine?

- Relief efforts are said to have saved the lives of seven million people at risk in Ethiopia. The relief effort was more powerful than the political obstacles, whatever their source.

- Relief efforts are impotent to change things; the Ethiopian people remain victims of their own bad government. No one has a plan to do anything about that.

- The continuation of the Ethiopian government in power, with its apparently unresolvable civil war and its collectivistic agricultural policies, greatly increases the likelihood of the recurrence of the famine.

None of those complications appear in the appeals issued by Geldof, USA for Africa, and most of the fund raising literature produced by the private voluntary organizations. News reports carry word of the political conflicts, but even allegations that 100,000 people were the victims of Ethiopian oppression under its relocation and resettlement plans failed to stop the effort to provide assistance. The main thrust of the philanthropic effort was to bring immediate relief to the starving and homeless. Every other complicating issue was brushed aside. The unspoken goal seemed to be: Get food to them. Period.

Geldof said that he wanted to get food to them. He reflected a familiar skepticism about governments of all kinds when he said he wanted to get the help directly to the people. The image of relief efforts appears to be that of permitting people to starve while bureaucrats make designs of red tape. There appears to be some truth to it: the Government Accounting Office reported that there was a delay of five months between the first requests for food aid and the actual delivery of food to the docks in Ethiopia. Geldof and his Band Aid Trust directed their first funds to the purchase of trucks for the delivery of food. Volunteers put a high value on being effective; their goals are precise and simple and immediate, and they have little patience with established procedures. The new actors on the scene showed little respect for the established organizations; they wanted to create their own. They would hold down the costs by enlisting the help of other volunteers; they would get the food directly to the people by negotiating more effectively with the officials along the way; they would target their assistance to high priority needs (e.g., trucks); they would deal directly with the people. (Later on, they would make grants to indigenous organizations rather than to international ones.)

The high point of public consciousness was reached with the "Live Aid" concert simultaneously staged at Wembley Stadium in London and at John F. Kennedy Stadium in Philadelphia. The consensus is that the all-day telecast reached the largest audience in history. Estimates of the money raised reached $80 million. (Ireland had the highest per capita contribution.) The US effort added a domestic need to its agenda: USA for Africa would devote part of the funds raised to the needs of the poor in the United States as well as for the famine victims in Africa. The European versions remained focused on the African famine. By the time that "Hands Across America" occurred, the divided agenda was further complicated by competition among the performers. The Hands Across America event was scheduled on the same day as the international run for famine relief, organized by Geldof, that was held in Europe and elsewhere.

Several observations may be in order:

- Coalitions brought together by an emergency don't seem to hold together well over time. Other priorities divide attention and cause conflict.

- A rock promoter in California commented that with an array of performers like that assembled for the Live Aid concert he could produce an audience of that size without a famine. The cause didn't generate the audience; the entertainers did.

- Those who made the Ethiopian famine their first priority overlooked the people in need at home. The domestic claims for help are closer and more persistent as well as better organized. The distant problem seemed fated to lose place to the more immediate one.

- No one seems to know whether spectacular benefits recruit new contributors, especially among the young. The young lady who said, at the Live Aid concert, that "It's fun to have fun and do good at the same time," may not make another gift unless she is entertained royally for doing so.

- The most common question among professional fund raisiers is whether Live Aid and its long list of imitators have introduced a lasting change in the way funds are raised. The history of Farm Aid, now ended, may indicate that a life span of three or four years is the most that one should expect. (Others didn't even succeed the first time.)

Those who were there before the world discovered the Ethiopian famine and who will remain there through the ne one are the private voluntary organizations. More than a hundred of them belong to the coordinating organization InterAction. From InterAction's self-study, it appears that most PVOs want to be development rather than relief organizations. They are in the relief business because they have to be -- because their contributors want them to be. Only a few PVOs resolutely stay out of the relief field for policy reasons.

PVOs are also in the relief business (most of them) because the U.S. government provides them with large amounts of food supplies, using them as intermediaries in situations where one-to-one government relations are awkward or worse. This is true of religious as well as secular PVOs. Catholic Relief Services, Lutheran World Relief, Church World Service are leaders along the mainstream religious organizations in the field; Jehovah's Witnesses and the Seventh Day Adventists also have agressive programs. The new competitors are autonomous organizations; World Vision is the largest and was the most active in Ethiopia until forced to leave.

In Europe the PVOs are called NGOs -- nongovernmental organizations -- and Oxfam and Medecins sans frontieres are among the best known. The African famine reached the NGOs as it did the PVOs, but there were eleven NGOs in Ethiopia when the troubles became known worldwide (compared to four PVOs). The Europeans had less trouble with the Ethiopian government, and -- on the basis of comments made by the UN executive in charge -- were more cooperative than were the Americans. Evaluations of PVO and NGO performance in Ethiopia and elsewhere during the famine of 1984-85 fault the Americans for being too caught up in posturing for fund raising purposes as well as for not working as well together as they should. One central figure, however -- Kenneth Hackett of Cathloic Relief Services -- felt that the agencies worked better together in Ethiopia than they had anywhere during his long experience.

The relief mandate forces PVOs to be where the action is. Some rushed with unseemly haste into Ethiopia. PVOs were often forced to transfer staff from other crisis areas to be able to staff programs in the more visible and better publicized crisis in Africa. As one PVO administrator said, "Our whole concept of where need is depends on where the cameras are aimed."

o The sense of crisis and emergency and acute suffering seem to be the incentives for philanthropic response that work best.

- Appeals to pity tend to focus almost exclusively on children, or on children and their mothers. (There is almost an implication that men should be able to do something.)
- There is a low threshhold of the audience willingness to stay with such images. Audience-fatigue comes quickly, and it is followed by donor fatigue.
- The PVO dependence on relief crises to raise money may not work in the long run: "We can't expect to attract donors through guilt and then expect them to get excited about development."
- There is a shortage of experienced relief workers who are trained in handling emergency situations. Few people make their career in relief work.
- On the other side of the desk, too few grant makers, private or public, have a personal knowledge of what goes on in a refugee relief camp, or in a village struggling to recover from a famine.

The response to the Ethiopian famine in 1984-85 was a success. Millions of lives were saved. The response to the famine was also a failure: it had recurred. As pessimists argued during the first famine, relief efforts only postpone the change that must take place. Bad governments remain in power, their policies continue. Those who pursue military objectives look upon the sufferings of the innocent as part of the consequences of the war -- and the war is the other party's fault. The war goes on. People shift their attention to other things: by midsummer 1985 the famine had lost place to the struggle against apartheid in South Africa. People find themselves able to think of other things, including other more pressing problems. There is a sense that the intensity of the response to the Ethiopian famine was misplaced -- why did we think that was so important?

The famine is back. By late summer 1987, newspapers carried regular reports and even features about the approach of famine in Mozambique, Angola, Sudan, and Ethiopia. Government action to make food supplies available were taken early, but without the intense public pressure brought to bear in 1984. The public assessment of Ethiopia is mixed with its opinion of affairs in Africa generally: probably beyond help, possibly beyond hope.

The first response -- that of Bob Geldof and so many of the rest of us -- set records. The relief agencies were pushed to the limit. Many of them became overcommitted and suffered badly when contributions faltered and declined by late 1985. None of the appeals since then have approached the high levels of those inspired eight months between October 1984 and July 1985.

One of the participants in a seminar on the Ethiopian famine grew weary of it after 18 months:

> I come to this decision with regret because I always enjoy being with you for discussion of any subject. The fact is, however, that I am very busy [he is] and I am really not very interested in Ethiopia, or I should say, I think I've had enough of Ethiopia.

Weighed against my friend's fatigue is the determination of all those people who continue to work for agencies that bring aid to the suffering wherever they are. They call on us for help. Sometimes we respond with great enthusiasm, even generosity. But we can't be depended on.

If there is a lesson here, it is that one. The weakness of philanthropy is that it cannot see things through. The challenge to philanthropy is to find a way to convert the irregular energy of relief into the sustained dynamic of development.

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THE STUDY OF RELIGION AND THE THIRD SECTOR OF AMERICAN SOCIETY: THEORETICAL CONSIDERATIONS

by

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INTRODUCTION: THE NEED FOR STUDIES OF RELIGION AND THE THIRD SECTOR

Most of the scholarly analyses of voluntary associations in the United States that have been published in the last three decades pay scant attention to religious bodies.[1] This failure to look at religious bodies seems both odd and regrettable. For one thing, it is a sharp departure from some of the classic approaches to the study of voluntary associations.[2] And there is, as some of the many works on the third sector that disregard religious bodies admit, little theoretical justification for concentrating exclusively on secular associations: such a concentration is more a matter of convention than of logic.[3] It is, furthermore, hard to justify the convention by appeal to quantitative evidence, for statistical analysis shows that religious groups account for a highly significant portion of the voluntary activity in America: donations to religious organizations make up nearly three-quarters of the gifts made by individual Americans to nonprofit organizations; as much as one-half of all the time Americans donate to voluntary associations is given to religious organizations.[4] Nor is it clear that students of voluntary associations gain much analytical leverage by leaving religious groups out of their calculations. Indeed, ignoring the religious variable, as Estelle James has argued in another context, sometimes has precisely the opposite effect, obscuring far more than it clarifies.[5]

So it is encouraging to see that students of the third sector are now beginning to pay more attention to religious bodies. Virginia Hodgkinson, together with several of her colleagues at the Independent Sector, has begun to compile survey data on the role that religious voluntary associations play in contemporary American society. Robert Wuthnow, the Princeton sociologist, has launched a project that will compare religious voluntary associations in the United States with religious voluntary associations in other countries. A group of scholars associated with the Institute for the Study of American Evangelicals, in Wheaton, Illinois, has begun to explore the role that voluntary associations play in the creation and development of religious movements that cut across denominational boundaries.

All of these projects seem promising. But they hardly exhaust the possibilities raised by the rubric religion and the third sector. The present essay maps out, in a preliminary way, another possible approach to the study of religion and the third sector--an approach intended to supplement, not supplant, the approaches developed by scholars already at work on this topic.

TO WHAT DOES "THE THIRD SECTOR" REFER?

Considering the denotations and connotations of the phrase "the third sector" is a convenient way to begin sketching out the angle of attack I have in mind. Although the phrase is not yet enshrined in the American Heritage Dictionary, in Merriam-Webster's, or in the supplements to the Oxford English Dictionary, "the third sector" (which seems to have begun to enter our vocabularies by the middle 1960s) has now appeared in political polemic, in reports published by the United States government, in learned journals, and in scholarly books.[6] Certainly it is not the only phrase which is of use to scholars who examine what might also be called the "nonprofit sector" or the "independent sector." It does, however, have some clear advantages over its rivals. Unlike "nonprofit" it unambiguously excludes governmental agencies. Unlike "independent sector" it does not minimize the importance of the connections between the various sectors of modern societies.

The phrase "the third sector" has two primary meanings.. In its first sense, the term the third sector refers to all of the organizations in a given society that are voluntary associations. At first glance, of course, that sort of definition (which implies a model of society like the one in Table A) makes it appear as if someone has pulled a very old trick: defining a problematic phrase by bringing in an equally problematic one. But in this particular case,

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however, reality differs from appearance. As we move from "the third sector" to "voluntary associations" we move from a terrain with relatively few, to a landscape with many, scholarly landmarks. Voluntary associations attracted the attention of some of the founders of modern social inquiry.[7] Articles in standard reference works on the social sciences note that studying voluntary associations takes researchers to the heart of some of the central problems with which the social sciences are concerned.[8] And there is no raging controversy over what we mean by voluntary associations. The phrase refers to organizations in which membership is neither mandatory nor acquired by birth, which exist independently of the state, and which are not primarily concerned with making a financial profit.[9]

The second sense of the phrase the third sector--which is a good deal more complex than the first--is at base metaphorical. It takes certain values and practices that seem to have no special affinity for either modern capitalism or the modern nation-state and pictures those values and practices as occupying a particular space in society. It suggests a model of society like the one to be found in Table B.

This second sense of the term is more difficult to understand than the first sense is, and its meaning must therefore be unpacked with some care. The difficulties connected with this unpacking are lessened considerably, however, by a number of sociological and historical works--works that do not directly focus on the concept of the third sector, but which nevertheless illuminate its metaphorical meaning.[10]

These works suggest that the way modern women and men live their lives and view the world have both been profoundly influenced by two huge historical transformations. The origins of both transformations lie in sixteenth-century Western Europe. The first was the development of modern capitalism: an economic system characterized by wage labor, by centralized, private ownership of capital goods, by legal barriers to the state's appropriation of private property, and by a tendency to rely on the marketplace to determine the way that goods are priced and distributed. The second was the development of modern nation-states: large, centralized organizations exercising, within clearly delineated borders, monopolistic control over the principal means of coercion.

Few sociologists or historians contend that these two developments are all that distinguish sixteenth-century societies from twentieth-century societies. But a number of scholars, Charles Tilly for example, are willing to argue that those two developments played absolutely crucial roles in producing the most important changes that have taken place in the last four hundred years. Those developments were the engines, as it were, that drove the other processes that we associate with modernity.[11]

Whether or not these two huge transformations were, from an ethical point of view, good things is not a matter that lies within the bounds of this essay. But it does seem clear that in non-normative terms the modern nation-state and modern capitalism have both been great successes. Successful, first of all, geographically: they have now penetrated every corner of the globe. Successful, too, in bringing under their sway more and more of the day-to-day lives of the people of the modern world. It is foolhardy to speak of the commodification of everything or of the politicization of everything as though either process had literally been fulfilled. It would be just as foolish, however, to deny that those hyperboles point to transformations that have revolutionized the world.

And those hyperboles point, too, to transformations that have revolutionized the way we think. In societies where the nation-state and capitalism are deeply entrenched, people usually think of the state and capitalism as approximate embodiments of universal standards of rationality and efficiency, not as the products of human history. In cultures associated with such societies, values that cannot be expressed in either the first or the second sector tend to be seen as anachronistic or residual--or else as belonging to the "private sphere." In such cultures, those tasks that neither business nor government is geared to perform tend to be defined as marginal or even as trivial. And in such cultures it is extremely hard to say just what the third sector is. One seems, rather, to almost have to say what it is not. In other words, one has to define it in negative rather than in positive terms.

Indeed in such cultures even the polemics produced by apologists for the third sector often have a certain negative quality about them. Relatively few of these polemical works break completely from the regnant assumption that the state is the normal means to produce positive social change. They tend to argue, rather, that there are a few specific social tasks for which the state is a clumsy or inappropriate tool.[12] These polemicists assume in other words that the state is ordinary, the third sector extraordinary. And such polemics generally leave the impression that while the existence of the business sector needs no justification whatsoever, one must work rather hard indeed to make the case for the third sector.[13]

Yet people who are attached to values and practices that have no particular affinity for either modern capitalism or the modern nation-state are likely to conclude that the very processes that have made it difficult to conceive of the third sector in positive terms have made the continued survival of the third sector all the more important. For hypothetically at least it is in the third sector where alternative values and practices are most likely to find public expression. It is there that these persons are most likely to discover spaces that are neither governmental nor commercial. There these people may gather together to question the apparent certitudes of modernity, dream new dreams, and--perhaps--even work to make the other two sectors conflict less sharply with their own moral vision.[14]

Not much of the popular--and not all of the more scholarly--literature on the third sector distinguishes carefully between the two separate senses of the term the third sector; in a good deal of the literature, authors are continually switching back and forth from one meaning to the other. That alternation leads to a conflation of the two senses of the term. It leads, too, to a model of society like the one in Table C.

That table, and the conflation which it is supposed to represent, would seem to explain much of the rhetorical power of those polemics that tell us that America "needs a strong third sector." Once we begin to assume that voluntary associations do indeed embody alternative values and practices we are forced to either acknowledge their importance, or else argue that the modern nation-state and modern capitalism can fully express the entire range of potentially beneficent human values and practices.

But of course questions should naturally arise at just this point. Is the conflation legitimate? Is Table C defensible? In the 1970s, many reflective persons seem to have assumed that the answer to both questions was an unambiguous yes; there is, however, a growing awareness among the community of scholars that studies the third sector that the answer to both questions must be a resounding "no."[15]

It is worth noting in passing that it is not at all clear that all of the governmental bodies presently in existence actually embody the values and practices we associate with the modern nation-state. Nor is it obvious that all of the commercial associations in existence actually embody purely capitalist values. But the more important point for our purposes is that many of the voluntary associations in America seem to have been molded, to a stunning degree, by values and practices whose origins are in either capitalism or in the nation-state.

Of course that is too large a claim to demonstrate conclusively in a paper as short as this one. But surely it is not an absurd one. Scholars such as Lester Salamon, Alan Abramson, and Ralph Kramer have pointed out how dependent on state funds are those voluntary associations that deliver social services.[16] Studies of those sorts of voluntary associations demonstrate that they must almost always follow regulations drawn up by officers of the state and that they must sometimes take care to see that they do not behave in ways that offend the government. Thus it is not altogether clear that these particular agencies actually do embody values and practices that are truly alternative. Certainly, there is relatively little empirical support for the notion that bureaucrats in voluntary social service agencies necessarily behave in ways that differ dramatically from the behavior of bureaucrats in governmental agencies.

There is, on the other hand, a good deal of empirical evidence to support the claim that voluntary associations often behave in ways which conform fairly closely to models first worked out to explain the way that business corporations work. And of course there is a growing sentiment within the third sector that voluntary associations should wholeheartedly embrace entrepreneurial values and practices. Many of the leaders of voluntary associations are entirely convinced, as one recent publication put it that, "profit-making enterprise is a legitimate and necessary way of sustaining a nonprofit organization...."[17]

So it might well be that another model of the various sectors--a model like the one in Table D--is more helpful than the one in Table C. Table D implies several of this essay's main contentions. Scholars who study the third sector should avoid conflating the two senses of the term. But they should not ignore the issues raised by the second sense of the term, for that second sense really does take us to the heart of the potential importance of the third sector. Scholars should, rather, systematically examine the extent to which voluntary associations really do fulfill their hypothetical possibilities--examine, in other words, the extent to which alternative values and practices really are preserved and inculcated by voluntary associations.[18]

IMPLICATIONS FOR THE STUDY OF RELIGION AND THE THIRD SECTOR

When approached from this angle, the study of religion and the third sector will turn out, I suspect, to revolve around two key questions: (1) how have religious organizations shaped the development of the American state and of American capitalism?, and (2) how have American capitalism and the American state influenced the various religious bodies in America?

No strategy for studying religion and the third sector is free from all difficulty; the approach outlined in this paper is no exception to that rule. In the first place, it leads to a distressingly vast definition of what it means to study religion and the third sector: it defines the topic in a way that will tempt researchers to take up questions to which they cannot possibly give satisfactory answers.

Secondly, it forces researchers to rely upon a body of literature--works concerning the nature of the American state and American capitalism--that is not yet fully developed. Although there is a great deal of impressive literature on the history of capitalism in America, most of the theoretical literature on capitalism (much of which is, of course, quite polemical in nature) is not very impressive.[19] And we still have relatively few systematic explorations of the values and cultural outlooks associated with capitalism--matters of tremendous importance for scholars who are particularly interested in religion.[20] And though there are a number of sophisticated works that explore theoretical issues connected with the development of the modern nation-state, and a rich body of literature on the history of states in Europe and in some portions of the third world, the literature on the American state is surprisingly thin.[21] Scholars have told us a great deal about American politics; about the state, they have told us far less. Morton Keller's admittedly rather lame pun nicely summarizes the point. "To say that 'there is still much to be learned about the nature of the State in America' is ... a major underStatement. There is close to everything to be learned about the State."[22]

These two obstacles are not insurmountable. They do, however, have some important implications for researchers who adopt the approach to religion and the third sector outlined in this paper. They suggest, for instance, that the present moment is not a propitious one for scholars to try to write comprehensive accounts of the multifarious relationships between religion and the American state and American capitalism. This is, rather, a time when scholars should focus on more manageable topics. Those researchers who wish to look at a number of different religious groups should probably concentrate on a rather narrow span of time such as 1877 to 1896 or 1950 to 1980. Those who decide to adopt a diachronic approach would do well to focus on a single (and fairly well-defined) religious community like the Mormons or the Seventh-day Adventist.

Furthermore, scholars should carefully consider whether it would be wise to immediately take on the obviously crucial, but terribly difficult, task of directly assessing the ways in which religious traditions actually influenced--and were in turn influenced by--the development of the American state and American capitalism. It seems entirely possible that it would make more sense to begin by looking at the various ways in which religious groups in America have oriented themselves toward the marketplace and the state, and to the construction of a preliminary typology of those orientations. An initial focus on perceptions would in all likelihood end up shedding a great deal of light on the more basic question of the actual relations between religious traditions and the state and the marketplace. And such a typology would be of some value in and of itself, possessing some of the virtues--to mention a work with some weaknesses but many remarkable strengths--of the typology developed in H. Richard Niebuhr's Christ and Culture.

The sort of studies that I am calling for would almost certainly disclose a pattern of considerable complexity and great intrinsic interest. Many members of religious organizations in America have perceived a great deal of tension between their values and practices and the values and practices associated with the state and capitalism. Walter Rauschenbusch (the great theologian of the social gospel), Charles Taze Russell (the founder of the group that became the Jehovah's Witnesses), and Dorothy Day (the leader of the Catholic Worker Movement) are some of the first illustrations of this point that come to mind; other examples could be found in nearly every crevice of American religious history. It seems probable, then, that some religious voluntary associations have done a good deal to prevent American society from being entirely dominated by values and practices associated with either the state or capitalism.

Yet that is not the whole story, for there can be no doubt that the vast majority of all of America's religious bodies have themselves been infused--to varying degrees, of course--with values and practices that one would logically associate with either the state or capitalism. Students of religion in America have often commented, for instance, on the way that quasi-religious nationalistic sentiments such as those associated with "American civil religion" have influenced many of the religious organizations in America.[23] And the possible congruence between capitalism and certain forms of Christianity (graphically illustrated in recent months by newspaper stories on the way that certain television "ministries" are run) has been a subject of scholarly inquiry for nearly a century now.[24]

If, as I have argued, studying religion and the third sector naturally involves tracing out this pattern of attraction and repulsion, of contravention and coadjutancy, then the study of religion and the third sector is not (as most students of religion assume) a peripheral matter. Indeed the topic should be of interest to all those who study religious traditions in the modern world. Most of the approaches to the now old, but still important, question of what it means for a religious tradition to encounter modernity are beginning to fray. They tend to be vague, overly reliant on the secularization model, or overly idealistic.[25] If Tilly is right--if students of modernity do well to focus their attention on the nation-state and capitalism--then the study of religion in the third sector turns out to be absolutely fundamental. It turns out that when we ask "what is entailed in the study of religion in the third sector?" we might be asking a question surprising close to this: "what does it mean to study the relationship between religious traditions and modernity?" That question is not easy to answer. It is, however, too important to ignore.

TABLE A

First sector: governmental associations
Second sector: commercial associations
Third sector: voluntary associations

TABLE B

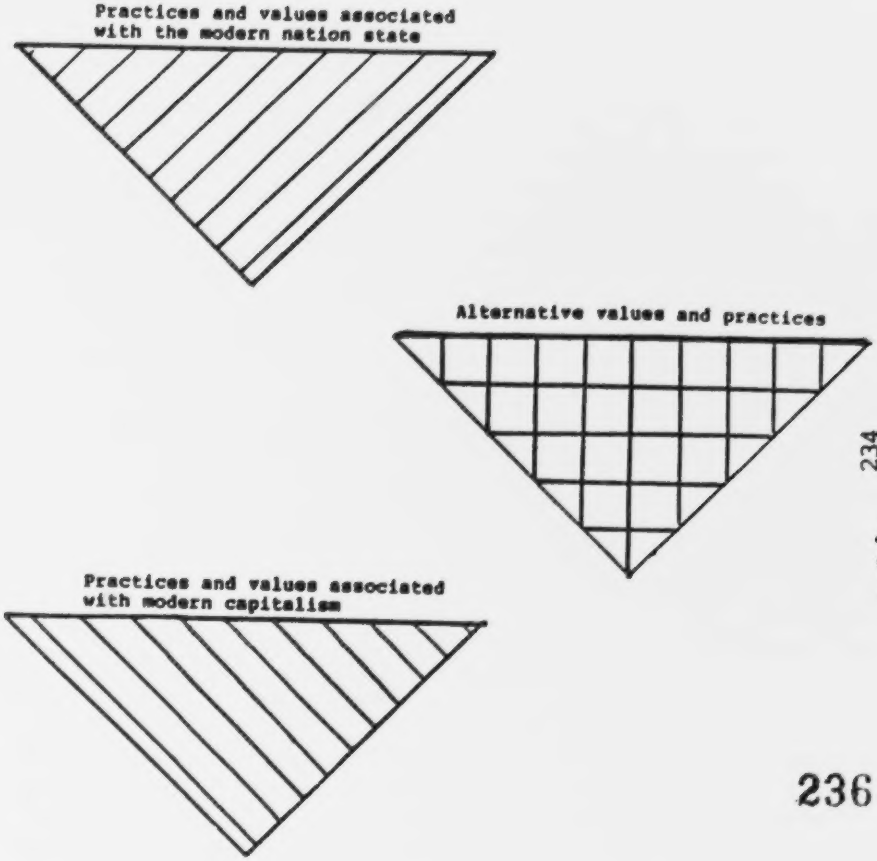

Practices and values associated with the modern nation state
Alternative values and practices
Practices and values associated with modern capitalism

TABLE C

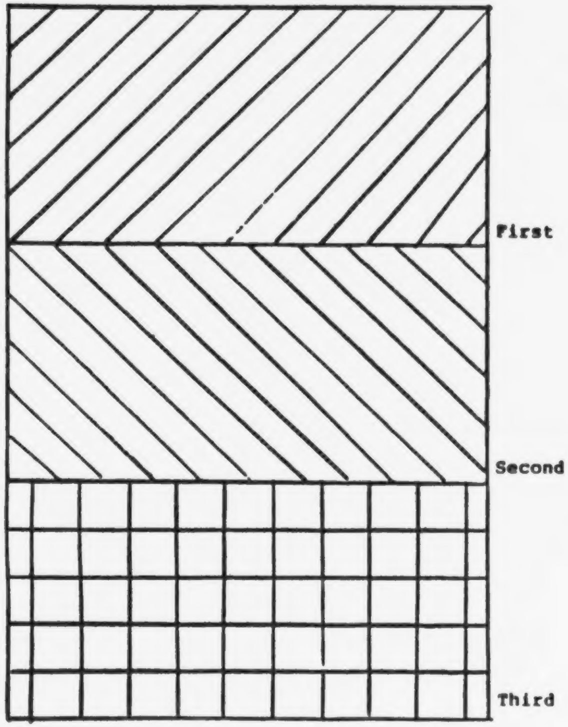
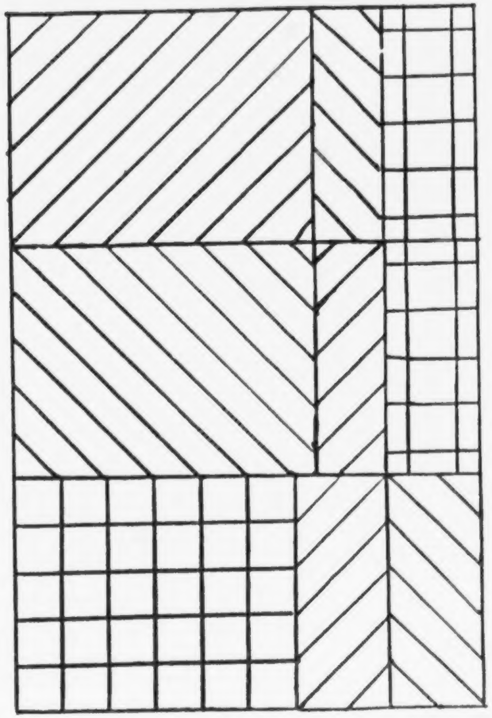

First
Second
Third

TABLE D



NOTES

1. Smith, 1983.

2. Weber, 1972; Tocqueville, 1966.

3. Sills, 1968.

4. Hodgkinson and Weitzman, 1986.

5. James, 1987.

6. For an early instance of a writer using the phrase the third sector as a synonym for the independent sector see Cornuelle, 1965, p. 29.

7. Weber, 1972; Tocqueville, 1966.

8. Sills, 1968.

9. Cf. Sills, 1968.

10. For useful syntheses of this literature see Giddens, 1981 and Giddens, 1985.

11. Tilly, 1985.

12. Nielsen, 1979.

13. Cornuelle, 1965.

14. Gamwell, 1984; Palmer, 1981.

15. Hall, 1987.

16. Abramson and Salamon, 1986; Kramer, 1985.

17. McNulty, 1983.

18. For a sharply contrasting approach, see Delaat, 1987.

19. Porter, 1980 illustrates the richness of the literature on the history of American capitalism. Two recent and interesting theoretical volumes on capitalism are Berger, 1986 and Heilbroner, 1985.

20. But see Bell, 1976.

21. Two useful guides to recent studies of the state are Thomas and Meyer, 1984 and Skocpol, 1985.

22. Keller's observation is quoted in Leuchtenburg, 1986, p. 594. Useful studies of the history of the American state include Keller, 1977, Skowronek, 1982, and Skocpol, 1980.

23. Gehrig, 1981 is a helpful introduction to the voluminous literature on American civil religion. 20. Wilson, 1986-1987 provides a series of bibliographies on the relationship between the state and religion in the United States.

24. A recent and lucid discussion of this question is Poggi, 1983. See, too, Lundén, 1988 and Primer, 1979.

25. Fenn, 1978 suggests some of the complexities involved in using the concept of secularization. Gerrish, 1978--a marvelous book--seems to me to rest upon an overly idealistic understanding of the nature of modernity.

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WORKING DRAFT

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MOTIVATIONS FOR GIVING AND VOLUNTARY SERVICE

by

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It is easy to feel overwhelmed by the topic of motivations for giving. Even a few days of inquiry leads ones into the thickets of

...sociobiology (Are studies of the transmission of altruism in infra-human species germane to understanding human actions?),

...economics (Charity, like taxes a form of wealth redistribution, is said to provide a benefit just from the joy of giving. How does one calibrate that joy of giving?)[1]

...religious/ethical thought (How does level of religious commitment relate to volunteering/giving?)

...sociological and anthropological research (How far does knowledge of the universality of norms of reciprocity go in describing individual motivation to give?) and

...clinical/developmental/social psychology (Is the development of a sense of equity, through social learning mechanisms, central to the choice of whom to help?).

This distressing overload is likely to lead one into a regression to simple models of motivation. The search for clarity amid this intellectual chaos itself motivates a disposition to strip away complexity in a search for order. Writing of another overloaded world, Walter Lippmann suggested that one of the benefits of stereotypes was that they kept us from dying of over-excitement.[2]

In a lovely essay from the Rockefeller Brothers Fund Annual Report (1985), Kendra O'Donnell noted, "We give because we are asked; we are more likely to give if we are asked in person; we are most likely to give if we are asked by someone we know. We give because we get something we value in return. We give because we are afraid of the consequences if we do not...[she adds additional reasons from the Yankelovich, Skelly and White (1986) study]: the belief that one gives to a worthy cause; a desire to help those in need or less fortunate than ourselves; close involvement, loyalty, personal experience with an organization; spiritual reasons. In addition, people report that they give because the gift can be automatically taken out of their salary. Many mention some particular thing about an organization -- its programs, the way it is run, its good work -- as a reason for giving."

After interviewing German Christians who helped Jews during the Nazi era, London (1970) observed,

> ...motives were still less easily classified than were activities -- because motives change, because they were conflicting, or because they were obscure. Some rescuers undertook the work deliberately and with benevolence aforethought, in utter secrecy sometimes, and with no possibility of outside help; others began it as an incidental part of other work, responding essentially to

> social pressure to participate and to social reinforcement for doing so; still others "fell in" to the rescue business thoughtlessly, mistakenly, or for irrelevant or selfish reasons. Some rescuers were fanatically religious, others were devout atheists. Some were deeply affiliated with Jews, others were anti-Semitic. And on and on.

The most famous rescuer in the London study was a German who devoted himself for almost four years, at great personal risk, to the rescue of some 200 people. He began his efforts with a mistaken idea of what it would all mean. With retrospective good humor, he reported, "I was believing in 1942 that the war will be another year. It cannot be any longer. It's impossible."

As daunting as all the jumble of sources of motivation and multiple paradigms are, a simple summary has come from our reading:

1. The critical behavior of volunteering and giving are overdetermined; there are multiple motivations for any single act of generosity.
2. The disposition to help, the "motivation to be socially responsible," in all its complexity and overdetermination, is an essentially universal characteristic.

There is, in short, a socially learned value of social responsibility present in all of us, and, to the degree that there is a problem explaining different levels of voluntarism and giving, it is not in a shortage of good intentions;[3] instead it is in a failure to realize or make concrete those intentions given an equally universal tendency: self interest. The form of giving may be culture specific and even idiosyncratic, but the disposition to give cuts across societies.

Rawlings (1970) treats altruism as a moral value within American society.

> people will conform to the social responsibility norm to the extent that they are aware of this ideal at the appropriate time and are motivated to adhere to it. (Rawlings, 1970, p. 164)

Much of what we label "social responsibility," that central value that so critically influences pro-social behavior, may be derived from another norm, that of reciprocity. Gouldner (1960) has observed, and no anthropologist we know disputes it, that the norm of reciprocity is universal across cultures.

The pressure felt to reciprocate -- whether it be dinner invitations, Christmas cards, or a friendly hello -- creates not only cordiality but a cooperativeness that has broad utility. Indeed, at the most basic level, one could agree with the socio-biologists that reciprocal altruism is at the core of the cooperative behavior necessary for the survival of humans. It would be hard to live in a cave, with a snarling band of saber-toothed tigers outside the opening, unless one were engaged in reciprocally cooperative help.

When one thinks of reciprocity, the tendency is first to cast it in the simple model of two people responding, more or less simultaneously, to each other's action (or anticipated action). In the simple case of Christmas cards, A and B exchange cards, possibly because they did so last year, possibly because each sees it as an appropriate thing to do, irrespective of last year.

One can add the dimension of time as a more explicit characteristic of the exchange, producing the crass-sounding idea of the account receivable. A owes B a card because he or she sent one last year (and A didn't). Or, A does a favor and becomes "owed" by B. There is a "call" for a reciprocating favor later. Note that these terms have a legalistic/financial tone -- that of a binding contract. While we all negotiate and have in force a large number of such contracts, it rather stretches credibility to describe the exchanges as benign acts of generosity.

(We cannot resist citing a maxim of Clarence Day's, brought to our attention by John Gardner: "If you don't go to other men's funerals, they won't go to yours.")

But now add in another feature -- that of a change in the actors. A favor is "owed," but it may not be able to be repaid to the person who provided it. That may be because that person is no longer available to receive the return favor, or that the source of the generosity is unknown.[4] The imbalance felt generates a pressure to act in a reciprocally generous way, and this now takes on a more satisfactory sense of generosity than the more primitive social exchanges mentioned earlier. The confluence of debt and responsibility powers the generous act.

An example from the Talmud: Honi Ha-Me agel, a miracle worker of the First Century, B.C., is observed planting a carob tree. The passerby asks,

> "How long will it be before it bears fruit?"
>
> "70 years."
>
> "Are you certain; you'll live another 70 years?"
>
> "As my forefathers planted for me, so I plant for my children."

So, in an over-simplification of this complex question of generosity, we are arguing that a sense of social responsibility, heavily fueled by the well-trained norm of reciprocity, yields a disposition to do good, to act on behalf of those in need, even if we don't owe them directly.

As we have taken, so shall we give.

MOTIVATION MEETS CONTEXT

If the road to Hell is paved with good intentions, there are detours on the pathway to charity and helpfulness. As Staub and others suggest, action takes place at the meeting between individual dispositions to be socially responsible and a context of awareness and interpretation of others' needs. The outcome of that meeting we label as generous or cheap, expansive or selfish. Motivation is intent aroused by uncertainty and imbalance. The action designed to fulfill the intention or to reduce the uncertainty is heavily conditioned by exogenous factors.

We should like to talk on two levels of analysis in discussing this interface between intention and environment. What are the social cues, largely provided by groups and organizations, that facilitate or discourage the actual delivery of help? Just as the behavior of giving is "pushed" by good intentions, it can be "pulled" by social cues that trigger awareness of need and the dependency of others on us.

The individual donor must make choices. Who to help? How much help? There is uncertainty on who is in need, who among the needy goes to the top of a priority list, and how one selects appropriate standards for specifying the amount or level of support.

Generosity reflects a transfer of assets, essentially a social transfer, with socially provided information central to the choices about the transfer.

In order to give, or to put some "cause" in a selection list, obviously there must be an awareness of need. The locomotive force of social responsibility cannot be engaged without a coupling to a need for help. A lack of coupling is suggested by the Yankelovich, Skelly and White (1986) finding that 14% don't give more to charity because they have not been asked.

The Influence of Groups

Groups and organizations play a central role in mediating volunteering and charity. The awareness of needs, and cues about priorities and appropriate magnitudes of giving, are significantly derived from the characteristics and actions of groups and organizations.

Let's look first at one of the characteristics -- the size or number of the groups. The size of the potential donor population influences the perception of just how dependent an individual or "cause" is on the donor. Since the early research of Latané and his colleagues, there has been interest in the topic of bystander intervention. Originally prompted by the Kitty Genovese murder in New York, the question was: how could so many witnesses to a tragedy not help? The answer, in good part, lay in the fact that there *were* so many.

Indeed, the expression 1/N, where N is the number of people who can help, is a reasonable way to estimate the likelihood of a bystander's helpful intervention. If you are the only person who *can* help out, the I/N expression becomes 1/1 and you will help (or so runs this model). If there is a large number of people who have the capacity or inclination to help, the likelihood that *you* will help declines.

1/N is an influence that derives from the number of potential helpers to a single actor or group in need. When the fraction is high, the uncertainty about coming to another's aid becomes low. Thus, there is little choice.

The effect of group size cuts two ways. Psychologists talk about social facilitation, in which a behavior, call it helping, is more likely to occur if many other people engage in this action; they also talk, in Latané's felicitous term, about social loafing, where the opposite effect holds. If there are many hands engaged in a common (or potentially common) job, one is less likely to exert full effort. There may be a social diffusion of responsibility (low levels of 1/N) or there may be social facilitation (modelling other's actions, seeing that something is defined by significant others as legitimate or doable.)

Consider two illustrations from sports. One of the first psychological experiments ever conducted was Triplett's (1897) study on bicycle racing. He showed the "rabbit" effect -- wherein a pace making companion creates a speed standard that is quicker than what the individual racer can achieve. The contrasting effect, the diffusion of social responsibility, is shown by a study of a rope-pulling contest in which the size of the teams was varied. As the number of team members increased, the amount of effort expended by the individual puller decreased.

The absolute number of requests for help provides another fraction. If all petitioners for help were of equal importance, and searched equal amounts of support, then the likelihood of help might be 1/R, where R is the number of requesters. Uncertainty will possibly increase with the absolute number of requests, which leads one to a weighting of R for the salience of each request.[5] There is some point where an accumulated mass of requests will flood the system and the response is "a plague on all your houses." This risk may be ignored by the solicitor, in the belief that "no asking" yields no chance for results.

How do we ration then? How do we edit among the multiple groups calling for help?

Again, social cues and characteristics of the group or organization are central. Perhaps the most parsimonious way to read the choice is to say that we are biased in favor of those groups which are close and which seem important to us. We contribute to those with whom we are connected.

We give support to those closely connected, in part because their dependency on us is high (1/N is high in a family). But other features count -- the similarity of the petitioner to us and the degree to which we are in a setting with a common fate outcome. We are more likely to help someone of our own "kind" and there is the maxim that we hang together or hang separately. (We help those we hang with!)

Charity usually begins at home because we are more likely to be aware of, and responsive to, those who are close and important. But a defining characteristic of the social responsibility motivation is an awareness of need and dependency. That condition may be located further away.

A Swedish clergyman recently reported to one of us on the substantial amount of money that had been provided in a Sunday collection for victims of the Ethiopian famine. He observed that members of the Church of Sweden, holding to social democratic political values and practices, expected the state to provide support for Swedes who were in need, so the problem wasn't at home, it was in Africa. If home is taken care of through state-controlled mechanisms, and one has a belief (value) that a salient group is the community of man, then the nearest needy population, however far away, is the one favored.

As the individual searches for social cues to reduce uncertainty, groups yield other signals. Groups can help reduce uncertainty about whom to help by providing legitimization to "third parties" in search of help. If a salient group (salient through similarity, respect, common fate, or whatever) specifies that another group or individual is worthy of support, the likelihood of helping is increased.

Note that this force can work the other way -- in the direction of dislegitimitization. When a solicitor is identified with groups who hold alien values, help is unlikely to be forthcoming.

Standards of Giving

The size and level of connectedness between donor and donee are two cues that help reduce uncertainty on the more general question of how much effort or support to provide. Norms, in both senses of that word, also provide guidance. There are the "ought" norms of social expectation (which can be as clear as a specified target amount, such as a tithe), and the "experience" norms (the level of giving behavior by other people).

There are cases where the standard for giving is clear. For the individual, this might be a tithing criterion; for a corporation, it might be the specified dues required to become a member of the local community's One Percent (or Two Percent or Five Percent) Club. Under these conditions, "how much?" becomes a non-question. Once the decision to participate in the group is made, the dues are set.

When one considers experience norms (what others, particularly like you, have given) the question gets a bit more complicated. When one knows what others have given (absent any fixed rule as in the first case), there is information, but not a decision. The further step must be taken of deciding on which of many decision rules should be applied to the choice of amount, given the knowledge. One could use a rule that says there is a socially practiced standard now known, and I give, more or less, what other people give. The behavior of others is a social model. But that information may be used as a basis for a level of giving that is in excess of that usual social practice. Thus the knowledge can be employed for social matching or for competitive excelling.

The publication by charitable and non-profit organizations of donor contribution lists, with amounts, is a double-edged signal. It both acknowledges support and provides information. This information can be used by donors (current or potential) to calibrate their gifts and to assess the degree to which a gift meets the decision rule of "meeting a community standard" or "excelling others" in charity.[6]

* * *

So we have argued for a view that centers on conflict of motivations (social responsibility vs. selfishness) and the interaction of motivational dispositions and a social context. Giving, to whom and how much, is a choice that is suffused with uncertainty, and the characteristics and actions of groups work to reduce uncertainty. We conclude that the universality and potency of the social responsibility norm is so great that there is less uncertainty on the "push" (motivational) side of giving than on the "pull" (social cue) side.

Meanspiritedness and generosity are thus products of good intentions engaging an uncertain world. They are not unique outcomes of motivations.

NOTES

[1] Psychologists should be indebted to Batson et al. (1986) for bringing to their attention a delightful story about Abraham Lincoln--one that illustrates the problem faced in attributing motivation to actions. "Mr. Lincoln once remarked to a fellow passenger on an old-time mudcoach that all men were prompted by selfishness in doing good. His fellow-passenger was antagonizing this position when they were passing over a corduroy bridge that spanned a slough. As they crossed a bridge they espied an old razor-backed sow on the bank making a terrible noise because her pigs had got into the slough and were in danger of drowning. As the old coach began to climb the hills, Mr. Lincoln called out, 'Driver, can't you stop just a moment?' Then Mr. Lincoln jumped out, ran back, and lifted the little pigs out of the mud and water and placed them on the bank. When he returned, his companion remarked: 'Now, Abe, where does selfishness come in on this little episode?': 'Why bless your soul, Ed, that was the very essence of selfishness. I should have had no peace of mind all day had I gone on and left that suffering old sow worrying over those pigs. I did it to get peace of mind, don't you see?' "

[2] One example of overly simplistic views is the perception that the driving motivation for the charitable giving of the 19th Century philanthropists, the Stanfords, Rockefellers, Carnegies and the like, was "philanthropy [as] a way of acknowledging guilt without being obliged to reform the system that had made these crimes possible." The view of Rockefeller, at least, is negated by the fact that he "...began his practice of tithing as soon as he earned his first pay."(Karl & Katz, 1987, pp. 14-15).

[3] Cialdini (1984) gives a particularly insightful and disciplined discussion of reciprocity and influence.

[4] For Maimonides, the anonymity of a gift escalated it on the scale of the quality of giving. For him, as for Aquinas, there was no question of not giving.

[5] Thomas Aquinas offered a scheme for weighting the degree of need. He proposed in his Summa that the needs of the recipient may be either extrema, gravis, or only communis. Aquinas asserted that the obligation to bestow alms is decided by reference to the capacity of the giver and the need of the recipient. It should be noted that both capacity and need are only in part "exogenous" or "objective;" Subjectivity reigns here, as elsewhere.

[6] A more extensive discussion of standards of giving would include commentary on such other criteria as "Give what you can" and "Even a dollar will help." This latter statement is interesting because of its linkage to the effect of individual commitment and "foot-in-the-door" tactics as influences on giving. Again, Cialdini (1984) is an excellent teacher on these topics.

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THE CHANGING AMERICAN FAMILY:
BALANCING THE NEEDS OF EACH GENERATION

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Carol J. De Vita
Research Associate
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The views expressed in this paper represent those of the author and not The Urban Institute.

THE CHANGING AMERICAN FAMILY:
Balancing the Needs of Each Generation

Over the past thirty years, American society has experienced considerable change in some of its basic social, economic, and demographic structures. The typical family no longer is composed of a husband who works, a wife who stays at home, and 3.2 children. In today's world you are more likely to find a family in which there are only one or two children and in which both parents work outside the home. Birth rates are down; divorce rates are up; and our general lifestyle patterns have changed substantially. More than 52 million women currently are in the labor force. Nearly 6 million households with young children are headed by a single woman. Two million households consist of unmarried couples living together, and over 8 million elderly persons (age 65 and older) live alone. Today the family unit takes a multitude of forms. It no longer looks as it did back in the 1950s and 1960s. Based on current statistics, many people have asked if the American family is in peril? Has the family abandoned its responsibilities to raise the young and care for the old? What programs and policies will be needed to strengthen the family and plan for the future? How can we balance the needs of the young with the needs of the old?

In order to understand these changes in American family life and to look ahead to the future, we need to start by looking at how our population has changed from the past. Increasingly we hear that America is an aging society--that the number of elderly has grown, that there will be relatively fewer young adults in the future to support tomorrow's older population, and that we will need to reassess our allocation of both public and private resources. Because sheer numbers of people often have an important impact on our social and economic institutions, it is important to begin by studying how the age structure of American society has changed over time and then to ask how these raw numbers will impact on the issues of intergenerational need in the years ahead.

The Changing Demographic Picture

In studying social change, demographers, policy analysts, social forecasters, and others are particularly interested in tracing the behavior and experiences of three distinct population groups (or cohorts) within our society--the baby boom cohort, the baby bust cohort, and the elderly. Researchers have been examining the relative well-being of these cohort groups, and many argue that the size and progression of these different groups through the life cycle have influenced, in large part, the course of social change.[1]

The largest of these three groups is the baby boom cohort, born after World War II when fertility rates soared to unanticipated and unprecedented levels. Demographers tend to date this period between 1947 and 1964 when, on average, more than 4 million births occurred each year and the total fertility rate jumped to over 3.0 births per woman. High and sustained fertility rates of this level had not been seen since the early part of the century.[2] Today, the baby boom cohort ranges in age from 41 to 24 years old. By contrast, the baby bust cohort is relatively small. These individuals were born during the 1970s decade when fertility rates dropped to approximately 1.8 births per woman. Members of this cohort now range in age from 9 to 18 years. The elderly cohort is composed of persons age 65 or older. Unlike the other two cohorts, the elderly cohort is defined here by the age of its members, not by a particular year(s) of birth. This means that with the passage of time, a new birth cohort enters the ranks of the elderly each year, continually adding new members to the group, while improvements in health care and medical technology increase the life expectancy of those already in the group.

The importance of these three segments of our population can be seen in the population pyramids presented in figure 1. The shape of these pyramids illustrates the effects of changing fertility, mortality, and immigration patterns over time.[3] Fertility rates determine the initial size of a cohort, but the effects of immigration and mortality will either increase or decrease the number of persons in the cohort group over time. The three population pyramids in figure 1 illustrate the relative impact that different birth cohorts have on the age structure of the population over a forty year period: 1960 to 2000.

In 1960 during the height of the baby boom, the U.S. population had a broad base of young children. Children under the age of 15 represented almost one-third of the total population. As we proceed up the age pyramid, we can see the relatively small size of the 1930s depression era cohorts (ages 20 to 29) when birth rates were moderately low, as well as the impact of mortality factors at the older ages. Indeed, the elderly portion of the population (persons age 65 and older) comprised less than 10 percent of the total population in 1960.

By 1980, the shape of the population pyramid begins to show signs of change as the population takes on the characteristics of an older age structure. Declining fertility rates and increasing life expectancy at the older ages narrowed the base of the pyramid and broadened the upper portions of the triangle. The baby bust cohort (ages 0 to 9) represented only 15 percent of the total population in 1980. The baby boom cohort, on the other hand, has matured to young adulthood (ages 16 to 33) and can be seen as the large bulge in the mid-section of the pyramid. Demographers have likened this bulge to "a pig in a python", symbolizing the baby boom cohort's enormous size and movement through the various stages of the life cycle. Meanwhile, the elderly population has grown to 11 percent of the total population.

Projecting ahead to the year 2000, the population pyramid no longer has a distinct triangular shape, but rather has become somewhat more rectangular in form. As fertility, mortality, and immigration factors are projected over time, profound changes occur in the relative size and growth of the various age groups within the population. For example, by 2000 the proportions of children (ages 0 to 9) and of elderly (ages 65 and older) will be roughly equal--14 percent and 13 percent, respectively. But the number of elderly will have increased nearly four times faster than the number of children during this twenty year period. Indeed, the fastest growing segment of the population will be among the very old (ages 80 and older), projected to increase by 95 percent between 1980 and 2000. Although this increase in the size of the older population would appear to be quite dramatic, it is only a dress rehearsal for what will follow in the next ten to fifteen years when the large baby boom cohort enters its retirement years around 2012.

Implications for Social Programs

Comparisons of the three population pyramids in figure 1 clearly show that society's age composition is strongly affected by variations in cohort size. In turn, many of our social and economic institutions are directly affected by this age distribution. Our recent history offers many examples of how the size of different cohorts has impacted and changed our social structures. Our schools and colleges, for example, have gone through a boom and bust period as the large baby boom cohort and subsequent baby bust cohort passed through the educational system. Marriages were delayed and births postponed as members of the baby boom cohort reached young adulthood and struggled to establish careers and compete in the job market. Indeed, labor statistics suggest that the flood of new job applicants in the late 1970s and early 1980s in part contributed to the high unemployment rates of that period. Businesses had to create thousands of new jobs in order to absorb the large numbers of baby boom workers. On the other hand, economists predict that the 1990s will see a shortage of young workers as the baby bust cohort reaches the work place. This should raise wage levels and increase disposable income for many households. At the other end of the age spectrum, the growth in our older population has affected a growing number of services and industries, notably the health care industry, the housing industry, and even the leisure/recreational industry. The challenge of an aging society is to identify and anticipate the needs and concerns of each age group, while recognizing the dynamics of demographic change.

Within this context, an on-going debate is unfolding about the fairness of current policies and programs for different age groups within our society. Many people fear that intergenerational inequities are developing and quickly point to statistics that show the growing number of children who live in poverty and the shrinking number of elderly who are poor. Although it is difficult to assess if the gains of one age group have been made at the expense of another, it seems unlikely that such a simple trade-off occurred. A recent study, in fact, shows that the improved status of the elderly is largely attributable to government programs, but that the rise in child poverty rates is more the result of market forces that would have occurred even in the absence of programs directed at improving the quality of life for the aged.[4]

Nevertheless, framing the issues of fairness and equity in terms of competition and conflict between the generations oversimplifies the problems facing an aging society and ignores the reciprocity of giving and receiving that occurs between individuals and generations over time. Studies of intrafamily transfers show that although the young and the very old are most likely to receive assistance from other family members, these age groups also are involved in giving. One scholar estimated that transfers within families in 1979 amounted to $709 billion, equivalent to 30 percent of the gross national product.[5] We must remember that our general quality of life is the result of policies and programs directed at all age groups within the population, and that each generation is affected by these policies either directly or indirectly at each point during the life cycle. Looking at the problems of an aging society from a life course perspective underscores the interdependencies that occur across generational lines rather than seeing each generation as an autonomous and independent entity.[6]

If we want to avoid the rhetoric of interest group politics that treats our future like a zero-sum game, then how should we formulate future service strategies? What services or programs would be appropriate for each of the three major cohort groups in our population? Three signficant questions must be addressed:

1. *Based on demographic projections that indicate the continued aging of our population, should we focus the bulk of our planning efforts on meeting the needs of the growing numbers of elderly?*

The answer to this first question is clearly no. As indicated above, there is a high degree of dependency and reciprocity between the generations so that focusing on the needs of only one age group in the population not only would be counterproductive but also politically unacceptable. The growing magnitude of the older population, however, cannot be ignored. Particular attention should be drawn to helping the oldest of the old--those persons age 80 and older. Gerontologists have shown that the need for assistance tends to increase with age and that persons age 85 and older are four times more likely than persons age 65 to 74 to require long term care services.[7] Given the projected increase among the very old by the year 2000, the pressures on our health care system and other social support services are likely to intensify.

In planning for the future, we must remember that there is great diversity within the older population. Although it is popular these days to depict the elderly as healthy, vigorous, and economically secure, there are hidden pockets of poverty among significant segments of the older population. Recent Census Bureau statistics show that nearly one-third of black elderly and one-quarter of Hispanic elderly live in poverty. One in every four older persons who lives alone is poor. In the future, we will need to abandon current stereotypes that portray the elderly as either all poor and feeble or all well-off and able. By recognizing the diversity that exists within the older population, we will be better able to target our services and help those who are most in need.

2. *Does the small size of the baby bust cohort mean that there will be too few workers in the years ahead to support a growing older population?*

The answer to this question also is no. The idea that the growing elderly population will be a "burden" on future cohorts of young workers is based on a crude, and somewhat misleading, demographic measure called the "aged dependency ratio". This measure shows that the number of older persons (age 65 and older) to all "working age" persons (age 18 to 64) is increasing. But it fails to take into account that the proportion of children in our population is declining. If the number of children is factored into the "dependency" measure, then at no time during the next 60 years will the total dependency ratio exceed the levels it attained in 1964 at the height of the baby boom.[8] Nonetheless, these ratios are simplistic measures that assume all older people are dependent and that all working age people are productive. More sophisticated economic constructs of dependency must be developed to test the arguments of intergenerational fairness and support "burdens".

What is really at issue, however, is the rising cost of maintaining a decent standard of living for all age groups in society. It is clear that we cannot afford to have an unproductive work force either now or in the future. But many of our current social indicators suggest that we are not preparing our children for the roles that they will assume in the years ahead. Declining educational test scores, increasing rates of teenage pregnancy and teen suicide, all suggest that we are failing as a society to meet not only current needs, but also future ones. From an intergenerational perspective, we cannot ignore the future of our children.

3. *What do the changing demographics mean for the baby boom cohort?*

As always, the baby boom cohort is the wild card in any attempts to forecast social change. Because of its enormous size, it has rocked the foundations of nearly every social and economic institution that it has come up against--our school systems, the job market, the housing market, even the institutions of marriage and family. But as a society, we have overcome the obstacles, adapted our lifestyles, and moved ahead.

As the baby boom cohort begins to settle into its middle-aged status, it faces new roles and responsibilities as workers, providers, nurturers, and caregivers. Having delayed childbearing in order to complete school and start careers, many baby boom couples now find themselves at ages 30 and 40 juggling the demands of jobs and babies. The growing concern with the availability, quality, and affordability of child care services will continue throughout the next decade as the baby boom cohort copes with the responsibilities of parenting. They also will begin to face the problems of long term care needs for their aging parents. We may find that the future demand for home health care services and other social support services for the elderly originates as much (or more) with the baby boom cohort as with the elderly themselves. It will be these middle-aged adults trying to fulfill their filial responsibilities to aging parents that will stimulate this demand. Already many businesses and corporations are reviewing their benefit programs to institute flexible work hours and flexible spending plans to enable employees to meet their family obligations. In the public arena, both political parties are making issues relating to "the family" a centerpiece for election year politics.

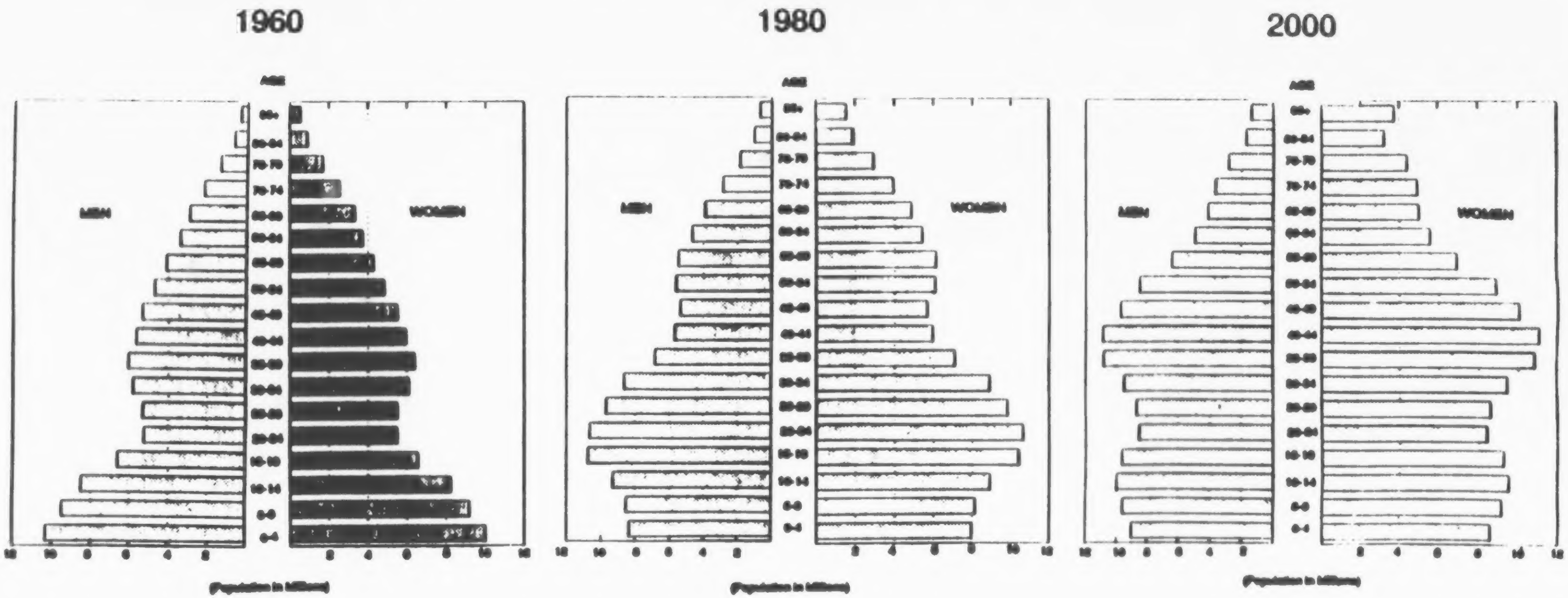
Conclusions

As we move towards the twenty-first century, we will begin to reaffirm our public and private support of the family as a sharing and caring institution. Our concept of the family unit will have changed to encompass a variety of lifestyles and household configurations, but the basic need within society to have a flow of resources and services across generations will be stronger than ever. There is very little evidence to support the notion that conflict between the generations will soon erupt. Instead, public opinion polls repeatedly show significant support across all generations for social insurance programs, such as Social Security and Medicare, that are based on intergenerational transfers. We need to be more concerned with the financial and funding mechanisms of these programs rather than with their intergenerational structure. Demographically, the total support "burden" in the future will be no greater than it was in the past. Arguments that an aging population slows economic growth and depresses savings and long term investments have not been fully supported by empirical evidence.[9] Further, these arguments ignore the possibility that research and technological breakthroughs can alter the course of future events.

Our society, today, faces a complex array of macroeconomic problems that must be addressed and debated in order to prepare for the future. These are complex issues that deserve thoughtful study. Contrary to popular notions, the future of an aging society does not have to be bleak. Each generation can be a resource and an asset for the other. We simply need to be more sophisticated in our assessment of social problems, more innovative in our planning of policies and programs, and more open to the inevitability of change.

FIGURE 1

U.S. POPULATION DISTRIBUTION



TOTAL POPULATION = 179,323,175

TOTAL POPULATION = 226,504,000

TOTAL POPULATION = 267,461,000

SOURCE: U.S. Bureau of the Census, 1980 Census, Detailed Characteristics of the Population, Table 48, and Series P-25, No. 997, Table 2.

NOTES

1. See for example, Richard A. Easterlin, Birth and Fortune, (Chicago: Chicago University Press, 1987); Ben J. Wattenberg, The Birth Dearth, (New York: Pharos Books, 1987); Greg J. Duncan, Martha Hill and Willard Rodgers, "The Changing Fortunes of Young and Old," American Demographics, August, 1986, pp. 26-33; Samuel H. Preston, "Children and the Elderly: Divergent Paths for America's Dependents," Demography, November, 1984, pp. 435-457; Leon F. Bouvier, America's Baby Boom Generation: The Fateful Bulge, (Washington, D.C.: Population Reference Bureau, 1980).

2. Beginning in 1917, there was a slow decline in fertility rates starting at 3.3 births per woman and going to 2.1 births in 1936. Fertility rates averaged around 2.4 during the early 1940s.

3. The population pyramids presented in this paper are based on U.S. Census Bureau data obtained from the 1960 Census and "Provisional Projections of the Population of States, by Age and Sex: 1980 to 2000," Current Population Reports, P-25, No. 937. The projected numbers are based on the assumptions contained in the middle series of national population projections prepared by the U.S. Census Bureau. These assumptions are that: 1) the total fertility rate will increase from 1.83 in 1980 to 1.96 in 2000; 2) life expectancy for males will increase from 70.7 in 1981 to 73.3 in 2005 and for females from 78.3 in 1981 to 81.3 in 2005; and 3) net migration rates will continue unchanged from the 1970-1980 decade.

4. See Richard A. Easterlin, "The New Age Structure of Poverty in America: Permanent or Transient?", Population and Development Review, June, 1987.

5. James N. Morgan, "The Redistribution of Income by Families and Institutions and Emergency Help Patterns," in Analyses of the First Thirteen Years of the Panel Study of Income Dynamics, volume 10 of Five Thousand American Families: Patterns of Economic Progress, ed. Greg J. Duncan and James N. Morgan (Ann Arbor, MI: Institute for Social Research, University of Michigan, 1983).

6. For a further discussion of this argument, see Eric R. Kingson, Barbara A. Hirshorn, and John M. Korman, Ties That Bind: The Interdependence of Generations, (Cabin John, MD: Seven Locks Press, 1986).

7. Kenneth G. Manton and Korbin Liu, "The Future Growth of the Long-Term Care Population: Projections Based on 1977 National Nursing Home Survey and the 1982 Long-Term Care Survey," as cited in Senate Special Committee on Aging, Developments in Aging: 1984, 99th Congress, 1st session, February 28, 1985, Senate Report 99-5.

8. See Barbara Boyle Torrey, "Technical Details on the Projection of Federal Outlays for the Older Population," Office of Management and Budget, Washington, D.C., 1981.

9. See Social Security: A Critique of Radical Reform Proposals, edited by Charles W. Meyer (Lexington, MA: Lexington Books, 1987).

WORKING DRAFT

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DEMOGRAPHIC TRENDS IN RELIGIOUS INSTITUTIONS: PRELIMINARY FINDINGS FROM A NATIONAL SURVEY OF THE ACTIVITIES AND FINANCES OF RELIGIOUS INSTITUTIONS IN THE UNITED STATES

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Demographic Trends in Religious Institutions: Preliminary Findings from a National Survey of the Activities and Finances of Religious Institutions in the United States

The relationship between religious philanthropy and charitable giving and volunteering generally in the United States is not clearly understood. However, surveys of American giving patterns reveal that over 70 percent of individual giving[1] and nearly half of all volunteer time[2] is given to religious organizations. Even when donations from religious institutions to hospitals, schools and other organizations is taken into account, 47 percent or $40.90 billion out of total giving of $87.22 billion in 1986 was given to religious organizations.[3]

The purpose of the INDEPENDENT SECTOR religion and philanthropy program is to stimulate research on the relationship of religion and philanthropy. The first stage of this project is to gather baseline data on the activities, finances, and expenditures of religious institutions in the United States.

Religious institutions are the third largest sector in the independent sector,[4] yet we really know very little about the size, scope and dimensions of this sector. Not only do religious institutions provide services to members of their congregations, but they also are donors to a host of religiously affiliated institutions and organizations as well as community organizations. The last major study of the receipts and expenditures of religious institutions was conducted in 1973 for the Commission on Private Philanthropy and Public Needs (the Filer Commission). That study was not really national in scope, for each of the major denominations (Roman Catholic, Protestant through the National Council of Churches, Jewish through the Council on Jewish Federations) completed separate studies for the Commission. More recently, the Council on Foundations sponsored a survey of religious and national religious organizations,[5] and Lester Salamon conducted a survey of religious congregations as part of the Nonprofit Sector Project to determine the impact of federal budget cuts on the provision of human services.[6]

The purpose of the current national survey of religious congregations is to describe the finances and activities of a national sample of local congregations, to determine the amount and kind of services provided to members, nonmembers, to religious or other organizations, and to determine the amount and purpose of voluntary service provided by congregations. One of the goals of the survey is to attempt to determine how much congregations serve their local communities through their members as well as to nonmembers. In follow-up research, we then hope to stimulate further exploration of the connection between church membership and giving for other than religious purposes.

Survey Design

In order to design a survey that would reach a sample of congregations in America, a national advisory committee was formed representing major denominations from the Buddhists to the Mormons and inclusive of the Roman Catholics, Protestants, and Jews. The committee also included a group of scholars studying various religions as well as those representing researchers of major groups in the independent sector.

This advisory group met to determine the scope and methodology of the survey and to design the questionnaire. The Gallup Organization, Inc. was selected to conduct the survey. The analysis of the major findings will be done by INDEPENDENT SECTOR with assistance from the advisory committee, and the tape of the whole survey will be made available to researchers and other organizations for further analysis and study.

The advisory committee decided that since the purpose of the study was to describe in aggregate form the activities and finances of religious institutions in the United States, that a national sample representative of all denominations would be selected, but not for any particular religious group. Therefore, the findings will be reported for major groups only--Roman Catholic, Protestant, and all others. In this way, smaller denominations are represented in the survey, but will not be individually analyzed since there will not be enough congregations from any one denomination to provide an adequate sample for a particular group.

The survey is being conducted in two and possibly three stages. The first part of the survey was conducted telephone to develop the national sample of 4,200 congregations. Representatives of congregations were asked a few questions relating to the date of founding of the congregation, the number of members and nonmembers, whether membership had changed over the last five years, and how they would report their congregation on a liberal to conservative scale. This part of the survey was conducted from May to November 1987.

The second stage of the survey currently in progress includes a mail questionnaire asking congregations a series of detailed questions on activities, finances, donation practices and amount and types of voluntary service. To date, approximately 30 percent of the sample has returned questionnaires. Pending the final response rate on questionnaires, a third stage of the survey may involve returning to nonrespondents by telephone to get the key information asked on the mail questionnaire. The findings of the full survey should be available in late June 1988.

The purpose of this paper is to report on the demographics of congregations in the United States as collected in the initial telephone survey.

Developing the National Sample

The challenge of developing a national sample because there is no recent census of congregations, nor an omnibus congregation directory led the advisory committee to decide to use the "Yellow Pages" of the various telephone systems throughout the United States (excluding Alaska and Hawaii).

All listings from these pages under "churches," "synagogues," "temples," and various similar listings like "clergy" were keystroked into a broad data base. All institutions with more than one listing with the same telephone number were placed on one record and the listings reduced to the central place of worship (for example, if a listing had "Baptist Church," "Clergy," Baptist Religious School" all at the same telephone number, the listing was reduced to simply "Baptist church"). All schools that had no "church" listing were also omitted from the population data base. This procedure produced a total of 294,271 unduplicated telephone listings. The geographical distribution of these numbers, and of the sample to be described in the next section are found in Table 1. There were 201,839 (or 68.6 percent) listed in metropolitan statistical areas (MSA), with 92,432 (31.4 percent) listings in nonmetropolitan statistical areas (nonMSA). There were 18 of these geographical areas.

Since we could not stratify the sample on any other measure other than metropolitan and nonmetropolitan statistical areas and 18 geographical areas conforming to U.S. census regions, many of the characteristics of congregations relating to size of membership, location in urban areas, level of finances had to be left to post-sample analysis. Therefore, each of the random samples were drawn in direct proportion to the population. If a contact was not made at the original call, at least 3 (and up to 5) call-backs were attempted. Following usual and standard procedures, call-backs were spread over different days and time periods. If, after all call-backs were attempted and there was no response, a substitution was made from within the same regional area and within the same geographical religious denomination. Thus, if a "Catholic Church" listing in the nonmetropolitan New England area could not be contacted, another Catholic church in the same area was substituted. Refusals were replaced in a similar fashion.

This procedure gave very satisfactory results. Table 1 shows no percentage difference between population and sample of more than 0.4 percent for any of the 18 geographical areas. Of course, more variation was found when dealing with individual religious groups. Random sampling within the 18 strata produced results that were reasonably consistent with the population values. For example,

Table 1

Yellow Page Listings
Unduplicated Number and Percent Distribution of Congregations
(Percentages in Brackets)

	Population		Sample	
Census Division	MSA	Non-MSA	MSA	Non-MSA
1. New England	6,099 (2.1)	1,259 (0.4)	89 (2.1)	21 (0.5)
2. Mid Atlantic	27,033 (9.2)	4,235 (1.4)	402 (9.6)	63 (1.5)
3. E. No. Central	41,174 (14.0)	15,965 (5.4)	593 (14.1)	236 (5.6)
4. W. No. Central	13,418 (4.6)	16,934 (5.8)	191 (9.5)	241 (5.7)
5. So. Atlantic	35,913 (12.2)	16,759 (5.7)	501 (11.9)	242 (5.8)
6. E. So. Central	13,787 (4.7)	10,898 (3.7)	194 (4.6)	160 (3.8)
7. W. So. Central	21,046 (7.2)	10,482 (3.6)	294 (7.0)	152 (3.6)
8. Mountain	10,846 (3.7)	9,845 (3.3)	150 (3.6)	136 (3.2)
9. Pacific	32,523 (11.1)	6,055 (2.1)	447 (10.6)	93 (2.2)
Total	201,839 (68.6)	92,432 (31.4)	2,861 (68.0)	1,344 (32.0)
Total	294,271		4,205	

Table 2 shows for the Catholic church both the population listings and the completed telephone samples for all 18 areas. In only three areas were differences recorded of more than one but less than three percent (18.0 to 20.4, 7.9 to 6.3, and 11.7 to 10.1). Overall, there were 19,931 Catholic churches listed, or 6.8 percent of all listings, while our completed sample had 368 Catholic churches, or 8.8 percent of the sample. This two percent average is due partly to sampling and partly to the availability and willingness to respond to the interviews.

Table 2

Yellow Page Listings
Catholic Churches
(Percentages in Brackets)

	Population		Sample	
Census Divison	MSA	Non-MSA	MSA	Non-MSA
1. New England	669 (3.4)	97 (0.5)	11 (3.0)	2 (0.5)
2. Mid Atlantic	3,080 (15.5)	481 (2.4)	58 (15.8)	11 (3.0)
3. E. No. Central	3,590 (18.0)	1,114 (5.6)	75 (20.4)	18 (4.9)
4. W. No. Central	1,236 (6.2)	1,161 (5.8)	22 (6.0)	23 (6.3)
5. So. Atlantic	1,446 (7.3)	349 (1.8)	29 (7.9)	6 (1.6)
6. E. So. Central	440 (2.2)	272 (1.4)	11 (3.0)	7 (1.9)
7. W. So. Central	1,584 (7.9)	518 (2.6)	23 (6.3)	9 (2.4)
8. Mountain	654 (3.3)	572 (2.9)	11 (3.0)	9 (2.4)
9. Pacific	2,327 (11.7)	341 (1.7)	37 (10.1)	6 (1.6)
Total	15,026 (75.4)	4,905 (24.5)	277 (75.3)	91 (24.7)
Catholic Churches	19,931		368	
All Congregations	294,271		4,205	
Percentage Catholic Churches	6.8%		8.8%	

Basic Data

Of all congregations, 29.4 percent were formed before 1900, 40.2 percent were formed between 1900 and 1960, and 26.1 percent were formed from 1961 to 1987. Table 3 shows the breakouts for the three major religious groupings that this report uses, Protestants, Catholics, and all others (see Appendix A for a description of "All Others" in the sample). The major difference is found in the "All Others" listings with fewer congregations founded before 1900 (only 21.9 percent) and more after 1960 (32.8 percent)

Table 3

Year Congregation Formed By Denomination

	Protestant		Catholic		All Others		Total	
Year	#	%	#	%	#	%	#	%
Before 1900	1,050	29.5	123	33.4	62	21.9	1,235	29.4
1900 - 1960	1,417	39.8	170	46.2	104	36.7	1,691	40.2
1961 - 1987	937	26.4	67	18.2	93	32.8	1,097	26.1
Don't know	150	4.2	8	2.2	24	8.5	182	4.3
Total	3,554	100.0	368	100.0	283	100.0	4,205	100.0
Mean years formed	1904	---	1893	---	1918	---	1904	---
Median years formed 1937	1937	---	1918	---	1948	---	1936	---

Nearly 70 percent of Protestant congregations and 80 percent of Catholic foundations were founded before 1960, while the largest growth period for nearly 70 percent of congregations has occurred since 1900, and 30 percent were founded since 1960.

Table 4

SIZE OF CONGREGATION MEMBERSHIP BY DENOMINATION

CONGREGATION SIZE	PROTESTANT #	PROTESTANT %	CATHOLIC #	CATHOLIC %	ALL OTHERS #	ALL OTHERS %	TOTAL #	TOTAL %
SMALL (LESS THAN 100)	707	19.9	6	1.6	45	15.9	758	18.0
MEDIUM (100 TO 399)	1,699	47.8	49	13.3	104	36.7	1,852	44.0
LARGE (400 AND OVER)	1,076	30.2	264	71.7	109	38.5	1,447	34.4
DK/NO ANSWER	74	2.1	49	13.3	25	8.8	148	3.5
TOTAL	3,554	100.0	368	100.0	283	100.0	4,205	100.0
AVERAGE SIZE OF MEMBERSHIP	413	...	2,200	...	677	...	571	...

More than half of all congregations (56.3 percent) had increases in membership, 24.0 percent stayed the same, while 17.2 had a decrease and 2.4 percent of respondents did not know, as shown in Table 5. Protestants and Catholics had similar growth patterns, while the "all other" group had 10 percent more, responding that they had an increase.

Table 5

Change in Congregation Membership
Compared with Five Years Ago by Denomination

Change	Protestant #	Protestant %	Catholic #	Catholic %	All Others #	All Others %	Total +#	Total %
Increased	1,975	55.6	209	56.8	185	65.4	2,369	56.3
Stayed the same	848	23.9	101	27.4	59	20.8	1,008	24.0
Decreased	642	18.1	51	13.9	32	11.3	725	17.2
Don't know	89	2.5	7	1.9	7	2.5	103	2.4
Total	3,554	100.0	368	100.0	283	100.0	4,205	100.0

More recently formed congregations reported more frequently increases in membership compared with five years ago than congregations formed during earlier periods (Table 6). The responses range from 48.2 percent for congregations formed before 1900 to 70.6 percent for those formed after 1960. For congregations formed in the in-between years (1900-1960), 53.5 percent indicated an increase in membership compared with five years ago.

Table 6

Change in Congregation Membership Compared with 5 Years Ago, by Year Congregation Formed

	Before 1900		1900-1960		1961-1987		Don't Know		TOTAL	
Change	#	%	#	%	#	%	#	%	#	%
Increased	595	48.2%	905	53.5%	775	70.6	94	51.6	2,369	56.3
Stayed the Same	375	30.4%	417	24.7%	177	16.1	39	21.4	1,008	24.0
Decreased	252	20.4%	344	20.3%	103	9.4	26	14.3	725	17.2
Don't Know	13	1.1%	25	1.5%	42	3.8	23	12.6	103	2.4
Total	1,235	100.0%	1,691	100.0%	1,097	100.0	182	100.0	4,205	100.0

Congregational Orientation

The respondents were asked to "describe your congregation or institution on a ten-point scale. If "1" means very liberal and "10" means very conservative, which number would best represent your congregation or institution?" Table 7 shows the results cross-tabulated by religious grouping, year that the congregation was formed, and by size of congregation.

Table 7

Self-reporting of Congregations on Ten-point Scale as Being Very Liberal to Very Conservative

		RELIGION			YEAR CONGREGATION FORMED			SIZE OF CONGREGATION		
	TOTAL	PROTE- STANT	CATH- OLIC	ALL OTHER	BEFORE 1900	1900 1960	1961- 1987	SMALL	MEDIUM	LARGE
TOTAL RESPONDENTS	4205 100.0	3554 100.0	368 100.0	283 100.0	1235 10C.0	1691 100.0	1097 100.0	758 100.0	1852 100.0	1447 100.0
SCALE										
(1) - VERY LIBERAL	87 2.1	69 1.9	6 1.6	12 4.2	23 1.9	38 2.2	24 2.2	17 2.2	38 2.1	29 2.0
(2) -	58 1.4	48 1.4	4 1.1	6 2.1	13 1.1	30 1.8	13 1.2	10 1.3	25 1.3	22 1.5
(3) -	182 4.3	154 4.3	19 5.2	9 3.2	62 5.0	70 4.1	48 4.4	32 4.2	76 4.1	71 4.9
(4) -	222 5.3	188 5.3	25 6.8	9 3.2	72 5.8	104 6.2	40 3.6	22 2.9	98 5.3	99 6.8
(5) -	720 17.1	564 15.9	119 32.3	37 13.1	252 2C.4	298 17.6	144 13.1	93 12.3	292 15.8	298 20.6
(6) -	406 9.7	339 9.5	48 13.0	19 6.7	156 12.6	156 9.2	78 7.1	45 5.9	177 9.6	175 12.1
(7) -	681 16.2	578 16.3	63 17.1	40 14.1	227 18.4	263 15.6	167 15.2	109 14.4	313 16.9	250 17.3
(8) -	815 19.4	722 20.3	38 10.3	55 19.4	219 17.7	353 20.9	214 19.5	170 22.4	383 20.7	247 17.1
(9) -	329 7.8	294 8.3	11 3.0	24 8.5	75 6.1	124 7.3	119 10.8	81 10.7	150 8.1	96 6.6
(10) - VERY CONSERVATIVE	464 11.0	411 11.6	12 3.3	41 14.5	78 6.3	182 10.8	175 16.0	134 17.7	214 11.6	99 6.8
DON'T KNOW	241 5.7	187 5.3	23 6.3	31 11.0	58 4.7	73 4.3	75 6.8	45 5.9	86 4.6	61 4.2

In order to have enough respondents for meaningful cross-tabulations, we condensed the ten-point self reporting scale of very liberal to very conservative as follows:

Scale and Assignment		Number	Percent
1-4	Liberal	549	13.1
5-7	Middle of the Road	1,807	43.0
8-10	Conservative	1,608	38.2
---	Don't Know	241	5.7
	Total	4,205	100.0

Please note that we included 815 congregations who answered "8" in the conservative group. A categorization based strictly on frequencies might have included this group in the "middle;" we felt that since "liberal" included four scale points and only yielded 13.8 percent, that the conservative grouping should have at least three scale points (8, 9, 10), even if it yielded a large percentage of congregations.

With this grouping, we see that part of Table 7 would be reduced as follows in Table 8.

Table 8

Condensation of Self-reporting of Congregations as to Their General Orientation

Grouping	Protestant		Catholic		All Other		TOTAL	
	#	%	#	%	#	%	#	%
Liberal (1-4)	459	12.9	54	14.7	36	12.7	549	13.1
Middle of the Road (5-7)	1,481	41.7	230	62.5	96	33.9	1,807	43.0
Conservative (8-10)	1,427	40.2	61	16.6	120	42.4	1,608	38.2
Don't Know	187	5.3	23	6.3	31	11.0	241	5.7
Total	3,554	100.0	368	100.0	283	100.0	4,205	100.0

For the liberal grouping, similar percentages apply for the three denominators, but a far larger percentage of Catholics classified their congregations as "middle of the road," 62.5 percent, than did Protestants, 41.7; or All Others, 33.9 percent. Of course, this means that respondents from Catholic congregations self-classified their institutions less frequently as conservative than did the others.

Conclusions

The significance of the demographics of congregations will become more clear when the rest of the survey has been completed. However, it is clear from congregational reports that church membership is increasing, that new congregations are being formed, and that the largest percentage increase in growth in membership is in other religions.

Notes

[1] Yankelovich, Skelly and White. The Charitable Behavior of Americans with findings by Virginia A. Hodgkinson and Murray Weitzman. (Washington, D.C.: INDEPENDENT SECTOR, 1986), p. 5.

[2] The Gallup Organization. Americans Volunteer 1985. (Washington, D.C.: INDEPENDENT SECTOR), 1986, p. 9. 9.

[3] AAFRC Trust for Philanthropy. Giving USA. (New York: AAFRC Trust for Philanthropy), 1987, p. 11.

[4] Interfaith Research Committee of the Commission on Private Philanthropy and Public Needs (1975). "A Study of Religious Receipts and Expenditures in the United States," in The Commission on Private Philanthropy and Public Needs, Research Papers, Volume 1, pp. 365-450.

[5] Jean A. McDonald. "Survey Finds Religious Groups Strongly Favor More Collaboration," Foundation News, Volume 25, Number 5 (September/October 1984), pp. 20-24.

[6] Lester A. Salamon and Fred Teitelbaum, "Religious Congregations As Social Service Agencies: How Extensive Are They?," Foundation News, Volume 25, Number 5 (September/October 1984), pp. 62-65.

Appendix A

Total Sample by Religion/Denomination

	All	Protestants	Catholic	All Others
Total Sample	4,205	3,554	368	283
Respondents Percent	100.0	84.5	8.8	6.7
Roman Catholic	---	---	X	---
Jewish	---	---	---	X
The Church of Jesus Christ of the Latter Day Saints	---	---	---	X
Buddhist	---	---	---	X
Other Religion	---	---	---	X
Jehovah Witnesses	---	---	---	X
Protestant Denominations	---	X	---	---

(---) Does Not Apply.

Sources

AAFRC Trust for Philanthropy. Giving USA. New York: AAFRC Trust for Philanthropy, 1987.

The Gallup Organization, Inc. Americans Volunteer 1985. Washington, D.C.: INDEPENDENT SECTOR, 1986.

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DATA COLLECTION PLANS FOR THE NONPROFIT SECTOR: WHAT DO WE NEED TO KNOW?

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DATA COLLECTION PLANS FOR THE NONPROFIT SECTOR: WHAT DO WE NEED TO KNOW?

1. Introduction: The Need for Better Data

An increased demand for data on the nonprofit sector has come from various sources in recent years. Nonprofit sector leaders, faced with declining government support and tax law changes which reduce the tax advantages to giving, require data that will allow them to more effectively target donors, while pursuing other sources of revenue, such as sales. In addition, Congress is confronting increasingly controversial policy issues regarding the nonprofit sector, such as the proper tax treatment of nonprofit commercial activities and limits on lobbying by nonprofit organizations. Third, the Internal Revenue Service is examining ways to facilitate administration of tax laws with respect to nonprofits. Finally, academic researchers--economists, lawyers, political scientists, sociologists and others--have shown an increased interest in the behavior of the nonprofit sector. All of these groups have been frustrated with the lack of a reliable and comprehensive data base for nonprofit organizations.

The need for improved data on the part of policy analysts is perhaps most clear in the case of the unrelated business income tax (UBIT). House Ways and Means Committee hearings in June and July 1987 focused on potential tax law changes to limit the extent of competition from nonprofits in activities traditionally carried out by for-profit firms. However, it is difficult to evaluate such changes without basic descriptive information, such as the extent and types of commercial activities engaged in by various categories of exempt organizations, or the number of nonprofits with for-profit subsidiaries.

Both Congress and the Treasury Department have been frustrated by the lack of information available. In testimony before the Ways and Means Committee, Assistant Treasury Secretary for Tax Policy O. Donaldson Chapoton stated that "the lack of detailed information about the exempt sector prevents us from fully evaluating changes that may appear appropriate from a purely theoretical or conceptual standpoint." 1/ Ways and Mean Oversight Subcommitte Chairman Pickle echoed this sentiment, saying that "it is clear we need better information regarding compliance and enforcement of the UBIT." 2/

The need for improved data has been made apparent in other policy contexts as well. For instance, during Senate Finance Committee hearings on the tax treatment of foundations, questions on the assets, income and expenses of foundations were forced to go largely unanswered. Recent restrictions on lobbying by nonprofit organizations also makes it imperative that a reliable data base on nonprofit expenditures be made available.

Investigation by the House Ways and Means Subcommittee on Oversight concluded that "the IRS isn't set up to identify lobbying or political activities violations very systematically, nor to act on allegations of misconduct in a timely manner.....While the Form 990 is quite lengthy, it is not very helpful to the IRS as an audit tool, nor very helpful to the public as a document disclosing actual tax-exempt lobbying or political activities." 3/

At an even more basic level, our lack of understanding of the behavior of nonprofit organizations in general greatly limits our ability to make policy prescriptions. Such understanding is dependent on the availability of extensive, reliable data. Simply assuming that nonprofits will respond to policy changes in the same manner as would for-profit firms is probably not satisfactory.

Finally, the difficulty involved in the administration of tax laws can also be illustrated by the UBIT. Only slightly more than 26,000 exempt organizations filed Form 990-T returns for unrelated business income in 1985, and the total tax revenue raised from the UBIT came to less than $40 million. (This compares to gross receipts of exempt organizations of over $250 billion in 1985.) It seems likely that a significant amount of unrelated income goes unreported by exempt organizations. Last year, the IRS randomly audited 3,000 Form 990-T returns, and found that one-third had deficiencies of between 30 and 50 percent. 4/ These audits were based solely on information supplied on the Form 990; there is no independent audit program for the Form 990-T. Improved data collection would allow the exempt organization examination personnel to develop a more systematic approach to selecting exempt organization returns for audit.

The remainder of this paper describes the data collection plans of the Statistics of Income (SOI) Division of the Internal Revenue Service. We begin, in Section 2, by decribing the statistical studies undertaken by SOI in recent years. In Section 3, we discuss potential expansion of and improvements in data collection and analysis. Finally, we propose changes in the tax forms filed by nonprofit organizations in Section 4.

2. The Curent Data Collection Program

The IRS has two methods of data collection in the tax-exempt area. First, some data are gathered from the population of all exempt organization returns. These data are processed for administrative purposes to a master file of records. While most information from the income statement is captured, only a few items from the balance sheet are gathered. The information on this master file is subject to only limited testing, so that its quality is questionable.

Second, the Statistics of Income Division of IRS has conducted a number of studies of exempt organizations in recent years, all based on samples of returns. All income statement, balance sheet and other financial data as well as most of the non-financial information on the exempt returns are collected for SOI studies. These data are subject to detailed testing and error correction procedures to ensure that the data are of high quality. These data are, therefore, appropriate for analytical purposes.

SOI conducted studies of private foundations in 1974, 1979, 1982 and 1983. Nonprofit charitable organizations--those exempt under 501(c)(3) other than private foundations--were studied in both 1982 and 1983. A study of all organizations exempt under Section 501(c) was conducted in 1975. In 1984, planned studies of nonprofit charitable organizations were cancelled due to budgetary constraints. These studies have been restarted for 1985 and it is hoped that they will be continued on an annual basis. A study of tax-exempt farmers' cooperatives was conducted (in conjunction with the Department of Agriculture) in 1977. Finally, non-exempt charitable trusts and split-interest trusts were analyzed in 1979.

Selected Results from Past Studies

The 1983 Nonprofit Charitable Organizations Study was based on a random sample of 1983 unaudited information returns (Form 990) stratified by asset level. 5/ Returns reporting $10 million or more in assets were selected at a rate of 100%, while smaller organizations were sampled at declining rates. Resource constraints necessitated a small sample of approximately 5,000 returns. Despite this relatively small size, the study provided much information of interest to nonprofit sector leaders, policy-makers and academicians alike.

One general result of the 1983 study is the heavy reliance that nonprofit charitable organizations have on program service revenue, as opposed to contributions from either private donors or government. In 1983, program service revenue accounted for an estimated $147.5 billion, or two-thirds of total nonprofit sector revenue. Some of this represents revenues from activities in which nonprofits compete with for-profit firms, and such competition has been of increased concern to policy-makers as well as to leaders of the small business community.

The importance of various revenue sources varies by size of organization. Charitable organizations with less than $100,000 of assets relied on contributions for 65 percent of their total revenues, while contributions accounted for only 12 percent of the revenues of organizations with more than $50 million of assets. For hospitals, which represented almost half of total assets in the sample, contributions make up only 2 percent of revenues. On average, contributions accounted for 21 percent of total revenues of 501(c)(3) organizations. Of those contributions, 52 percent came from government grants, up from 46 percent in the 1982 study. Thus, even in the light of cutbacks in federal support for social welfare programs, the government continues to be a major source of revenue for charitable groups.

The 1983 Private Foundations Study indicates that revenue for these organizations increased by 78 percent over 1982, due largely to a dramatic increase in the sale of capital assets. In total, an estimated 29,863 foundations spent $5.2 billion for charitable purposes in 1983, with 85 percent of this being grants to other tax-exempt organizations. Approximately 80 percent of all nonoperating foundations made qualifying contributions in excess of the minimum required by law.

Given this type of information, one can begin to piece together a picture of the nonprofit sector. However, the statistical studies, despite their high quality, have had a number of shortcomings. First, as noted, samples have been quite small. This is a problem in particular for analyzing subgroups, such as particular nonprofit industries. In addition, samples have been stratified by the assets of the organization. Thus, they tend to provide more reliable information for large than small organizations. Stratifying by assets has also had the effect of oversampling hospitals and universities. Previous samples have also typically been narrow in their focus. SOI studies have primarily focused on 501(c)(3) organizations. There has not been a study of all 501(c) nonprofits since 1975. This has not been due to a lack of interest in the other types of exempt organizations; rather, SOI has been constrained by the limited financial resources available to the exempt statistical program. Finally, studies have not been carried out on a regular basis. Thus, it has not been possible to develop a reliable time series data base for many variables of interest. In addition, it has not been possible to follow organizations over time, in order to construct a panel of data.

The proposed improvements in data collection and nonprofit tax form design aim to address these shortcomings. We turn first to the proposals for improved data collection.

3. An Improved Data Collection Program

An improvement in the data collection program for exempt organizations could proceed either by expanding the scope of information captured from all returns for the master file or by enhancing the statistical program. The former approach, however, would be prohibitive in cost. This approach would also suffer from the problem that master file data are not as reliable as one would like. A study of the master file data, with SOI data as the quality standard, indicated that approximately 50 percent of the records contained at least one error. This would greatly limit the usefulness for either tax administration or policy analysis of an expanded master file.

An expansion and reorientation of the exempt organization statistical program would be preferable. It would be far more useful to have a complete and reliable data set for a significant, scientifically designed sample of exempt organizations than a set of questionable data on a more limited number of items for the population of all such organizations.

The Statistics of Income Division and the Office of Tax Analysis have proposed the following improvements in the data collection program:

o Studies of private foundations and nonprofit charitable organizations would be conducted on an annual basis.

Conducting these studies on an annual basis would allow the development of a panel of data which would be of great use in learning about the behavior of exempt organizations. Annual studies would allow SOI to estimate changes over time in certain key variables not currently available from the master file. This would enable us to learn how the role of foundations and other nonprofit organizations has been changing, whether the importance of various revenue sources--such as commercial activities--has been changing in systematic ways, etc.

o Sample sizes for both the private foundation and nonprofit charitable organization studies would be increased. The private foundation sample would increase from 1,700 returns for Tax Year 1985 to 5,000 for Tax Year 1989 and beyond. The sample of nonprofit charitable organizations will grow from 5,000 returns to 35,000 by Tax Year 1988. (See Attachment for details.) Larger samples would be of particular use for examining subsectors of the nonprofit sector, and for generating reliable data on small organizations.

o Sample selection criteria would be changed. Stratifying the sample by assets leads to an over-representation of hospitals and universities. We have proposed to stratify the sample based on receipts and subsection code as well as assets.

o Beginning with Tax Year 1988, the exempt organization study would be expanded to include all 501(c) organizations, rather than just 501(c)(3) charities. This would allow us to get a far more complete picture of the nonprofit sector. Many of the most pressing policy issues involve other than c(3) organizations. For instance many nonprofits that apparently receive significant amounts of commercial, and potentially unrelated, income, such as trade associations are not c(3) organizations.

o The study of exempt organization unrelated business income (Form 990-T), which is being conducted for the first time for 1987, would be conducted annually. This will remain an area of interest for some time to come. Annual studies of the Form 990-T returns would allow matching of these returns with the organizations' Form 990 returns. Basic questions could then be answered, such as what sorts of nonprofit firms are most likely to engage in unrelated business activities.

o Studies of farmer's cooperatives, charitable and split-interest trusts and exempt organization excise taxes would be conducted at least once every three years.

A proposed timetable for the completion of these proposed studies is included as part of the Attachment.

4. Improvements in Nonprofit Tax Forms

For the data collection improvements just described to be of maximum benefit, it must be ensured that the data that are of greatest interest are available from the tax forms filed by exempt organizations. At the same time, we must be careful not to make reporting requirements onerous for nonprofit organizations, particularly smaller ones. The following changes in those forms have been recommended:

o Activity codes would be added to Forms 990 and 990-PF. These activities should be self-coded by the exempt organization and should be based on the system of classification developed by the United Way. In addition to the activity codes, a written description of the principal activity should be required, and the organization should be asked to indicate whether its activities have changed from the previous year.

This addition will provide a more complete description of what an organization does, allowing greater disaggregation of the nonprofit sector. The disaggregation would improve our ability to target samples in areas of particular interest. In addition, it would enable us to better understand the forces that lead a nonprofit to change its primary activity.

o Unrelated business activity codes from the Form 990-T would be abstracted from the master file system. This would enable us to match organizations' Form 990 activity codes with their unrelated business codes, thus identifying common combinations of activities. We could, for instance, determine whether there are large numbers of universities in publishing, hospitals with drug stores, etc. It is likely that there are a small number of exempt/unrelated activity combinations which dominate the picture. The matched data would also aid in understanding the behavior of nonprofits engaged in unrelated activities.

o A new schedule would be added to the Form 990, for summary information from for-profit subsidiaries and other nonprofits to be provided. Much of the income earned by nonprofits from unrelated activities is earned by for-profit subsidiaries, and there are important and difficult issues of cost allocation between exempt and for-profit activities. Additional information regarding affiliation with other nonprofits would be of use in understanding lobbying and political activities.

o A new schedule could be added for transactions between exempts and their controlled organizations.

o Some reporting should be required of commercial activities of nonprofits that are claimed to be related to their exempt purpose. Much of the recent concern over "unfair competition" involves activities the income from which never appears on a Form 990-T. Taking a broader view, by monitoring all commercial activities of nonprofits--whether currently considered unrelated or not--would allow more effective auditing of nonprofits, particularly those not filing a Form 990-T. At present, only the commercial activites of exempt organizations that file a Form 990-T are audited.

It is important to separate sales to individuals of non-program related goods or services from both sales of program-related goods and services to individuals and sales to government via purchases-of-service contracts. Sales of non-program goods and services should be included in a broad measure of commercial, though not necessarily legally "unrelated," activities. Part 1, line 10a, of the current Form 990 "Gross sales minus returns and allowances" attempts to pick up legally related commercial activities, while program revenues, from government or individuals, is meant to be recorded on line 2. The distinction between commercial and program-related sales should be made clear in the instructions for the 990. In addition, it would be desirable to have separate lines for program service revenue from individuals and program service revenue from government. Government purchases of service are more like contributions or grants, in that a third party (here the government) finances some service provided to a client.

o The possibilty of separate schedules added to Schedule A of Form 990 for universities and hospitals should be considered. These types of nonprofits have been the focus of much of the controversy regarding unrelated business income. The advantage of having separate schedules is that the organizations could be asked about specific commercial activities. For instance, on the university tax return, the organization could be asked whether it operated a travel service, bookstore, etc.

Footnotes

1/ House Ways and Means Subcommittee on Oversight hearing, June 22, 1987.

2/ Letter from Oversight Subcommittee Chairman Pickle to Ways and Means Committee Chairman Rostenkowski, July 17, 1987, cited in Daily Tax Report, July 23, 1987, G-3.

3/ House Ways and Means Subcommittee on Oversight hearing, March 12, 1987.

4/ According to Howard Schoenfeld of IRS, at the IRS Commissioner's Advisory Group on Exempt Organizations meeting, September 16, 1987.

5/For details, see Cecilia Hilgert, "Nonprofit Charitable Organizations, 1983," Statistics of Income Bulletin, 1983, p.36.

Attachment

SOI Studies of Tax Exempt Organizations Measures of Population, Sample, Completion Dates, and Cost Estimates by Tax Year

	1985	1986	1987	1988	1989	1990	1991	1992
Organizations Exempt From Income Tax (Form 990)								
Population	100,000 1/	107,000 1/	115,000 1/	353,100 2/	359,500 2/	365,900 2/	372,200 2/	378,300 2/
Sample	5,500	5,500	8,000	35,000	35,000	36,000	36,500	37,000
Data Capture								
Start	1/88	11/88	11/89	3/90	3/91	3/92	3/93	3/94
Finish	12/88	10/89	3/91	8/91	8/92	8/93	8/94	8/95
Tape and Tabulations	3/89	1/90	6/91	11/91	11/92	11/93	11/94	11/95
Staff Years	8.7	8.7	11.5	23.8	25.0	25.0	25.0	25.0
$ Amount	$270,000	$270,000	$355,000	$735,000	$770,000	$780,000	$790,000	$800,00
Private Foundations (Form 990PF)								
Population	29,300	29,000	30,000	30,400	30,700	31,100	31,500	31,900
Sample	1,700	1,800	3,900	3,900	5,000	5,000	5,000	5,000
Data Capture								
Start	1/88	10/88	10/89	7/89	10/91	10/92	10/93	10/94
Finish	7/88	6/89	6/90	4/91	6/92	6/93	6/94	6/95
Tape and Tabulations	10/88	9/89	9/90	7/91	9/92	9/93	9/94	9/95
Staff Years	5.1	5.5	8.0	7.5	7.5	7.5	7.5	7.5
$ Amount	$160,000	$170,000	$250,000	$230,000	$260,000	$265,000	$270,000	$275,00
Exempt Organization Business Income Tax (Form 990T)								
Population	--	--	28,500	29,300	30,100	30,900	31,600	32,400
Sample	--	--	5,000	5,500	6,000	6,500	7,000	7,500
Data Capture								
Start	--	--	10/88	6/89	6/90	6/91	6/92	6/93
Finish	--	--	5/89	7/90	7/91	7/92	7/93	7/94
Tape and Tabulations	--	--	8/89	10/90	10/91	10/92	10/93	10/94
Staff Years	--	--	10.5	11.5	12.0	12.0	12.5	12.5
$ Amount	--	--	$325,000	$355,000	$370,000	$375,000	$385,000	$390,000

SOI Studies of Tax Exempt Organizations: Measures of Population, Sample, Completion Dates, and Cost Estimates by Tax Year--continued

	1985	1986	1987	1988	1989	1990	1991	1992
Nonexempt Charitable Trust (Form 990PF)								
Population	--	--	--	--	30,000	--	32,000	--
Sample	--	--	--	--	3,000	--	3,500	--
Data Capture								
Start	--	--	--	--	10/91	--	10/93	--
Finish	--	--	--	--	6/92	--	6/94	--
Tape and Tabulations	--	--	--	--	9/92	--	9/94	--
Staff Years	--	--	--	--	7.5	--	7.5	--
$ Amount	--	--	--	--	$215,000	--	$220,000	--
Split-Interest Trusts (Form 5227)								
Population	--	--	--	--	3,000	--	--	3,000
Sample	--	--	--	--	3,000	--	--	3,000
Data Capture								
Start	--	--	--	--	TBD	--	--	TBD
Finish	--	--	--	--	TBD	--	--	TBD
Tape and Tabulations	--	--	--	--	TBD	--	--	TBD
Staff Years	--	--	--	--	7.5	--	--	7.5
$ Amount	--	--	--	--	$150,000	--	--	$160,000
Excise Tax on Charities (Form 4720)								
Population	--	--	--	--	1,000	--	--	1,250
Sample	--	--	--	--	1,000	--	--	1,250
Data Capture								
Start	--	--	--	--	TBD	--	--	TBD
Finish	--	--	--	--	TBD	--	--	TBD
Tape and Tabulations	--	--	--	--	TBD	--	--	TBD
Staff Years	--	--	--	--	3.5	--	--	3.5
$ Amount	--	--	--	--	$110,000	--	--	$115,000

SOI Studies of Tax Exempt Organizations Measures of Population, Sample, Completion Dates, and Cost Estimates by Tax Year continued

	1985	1986	1987	1988	1989	1990	1991	1992
Farmers' Cooperatives (Form 990C)								
Population	--	--	--	--	6,000	--	--	6,000
Sample	--	--	--	--	6,000	--	--	6,000
Data Capture								
Start	--	--	--	--	TBD	--	--	TBD
Finish	--	--	--	--	TBD	--	--	TBD
Tape and Tabulations	--	--	--	--	TBD	--	--	TBD
Staff Years	--	--	--	--	4.0	--	--	4.0
$ Amount	--	--	--	--	$125,000	--	--	$135,000

1/ 501(c)(3) Organizations only; 1986 will have redistributed sample to obtain a better representation of social welfare organizations.
2/ Includes all subsection codes
TBD To Be Developed

Attachment

SOI Studies of Tax Exempt Organizations. Measures of Population, Sample, Completion Dates, and Cost Estimates by Tax Year

	1985	1986	1987	1988	1989	1990	1991	1992
Organizations Exempt From Income Tax (Form 990)								
Population	100,000 [1]	107,000 [1]	115,000 [1]	353,100 [2]	359,500 [2]	365,900 [2]	372,200 [2]	378,300 [2]
Sample	5,500	5,500	8,000	35,000	35,000	36,000	36,500	37,000
Data Capture								
Start	1/88	11/88	11/89	3/90	3/91	3/92	3/93	3/94
Finish	12/88	10/89	3/91	8/91	8/92	8/93	8/94	8/95
Tape and Tabulations	3/89	1/90	6/91	11/91	11/92	11/93	11/94	11/95
Staff Years	8.7	8.7	11.5	23.8	25.0	25.0	25.0	25.0
$ Amount	$270,000	$270,000	$355,000	$735,000	$770,000	$780,000	$790,000	$800,00
Private Foundations (Form 990PF)								
Population	29,300	29,000	30,000	30,400	30,700	31,100	31,500	31,900
Sample	1,700	1,800	3,900	3,900	5,000	5,000	5,000	5,000
Data Capture								
Start	1/88	10/88	10/89	7/89	10/91	10/92	10/93	10/94
Finish	7/88	6/89	6/90	4/91	6/92	6/93	6/94	6/95
Tape and Tabulations	10/88	9/89	9/90	7/91	9/92	9/93	9/94	9/95
Staff Years	5.1	5.5	8.0	7.5	7.5	7.5	7.5	7.5
$ Amount	$160,000	$170,000	$250,000	$230,000	$260,000	$265,000	$270,000	$275,00
Exempt Organization Business Income Tax (Form 990T)								
Population	--	--	28,500	29,300	30,100	30,900	31,600	32,400
Sample	--	--	5,000	5,500	6,000	6,500	7,000	7,500
Data Capture								
Start	--	--	10/88	6/89	6/90	6/91	6/92	6/93
Finish	--	--	5/89	7/90	7/91	7/92	7/93	7/94
Tape and Tabulations	--	--	8/89	10/90	10/91	10/92	10/93	10/94
Staff Years	--	--	10.5	11.5	12.0	12.0	12.5	12.5
$ Amount	--	--	$325,000	$355,000	$370,000	$375,000	$385,000	$390,000

SOI Studies of Tax Exempt Organizations Measures of Population, Sample, Completion Dates, and Cost Estimates by Tax Year continued

	1985	1986	1987	1988	1989	1990	1991	1992
Nonexempt Charitable Trust (Form 990PF)								
Population	--	--	--	--	30,000	--	32,000	--
Sample	--	--	--	--	3,000	--	3,500	--
Data Capture								
Start	--	--	--	--	10/91	--	10/93	--
Finish	--	--	--	--	6/92	--	6/94	--
Tape and Tabulations	--	--	--	--	9/92	--	9/94	--
Staff Years	--	--	--	--	7.5	--	7.5	--
$ Amount	--	--	--	--	$215,000	--	$220,000	--
Split-Interest Trusts (Form 5227)								
Population	--	--	--	--	3,000	--	--	3,000
Sample	--	--	--	--	3,000	--	--	3,000
Data Capture								
Start	--	--	--	--	TBD	--	--	TBD
Finish	--	--	--	--	TBD	--	--	TBD
Tape and Tabulations	--	--	--	--	TBD	--	--	TBD
Staff Years	--	--	--	--	7.5	--	--	7.5
$ Amount	--	--	--	--	$150,000	--	--	$160,000
Excise Tax on Charities (Form 4720)								
Population	--	--	--	--	1,000	--	--	1,250
Sample	--	--	--	--	1,000	--	--	1,250
Data Capture								
Start	--	--	--	--	TBD	--	--	TBD
Finish	--	--	--	--	TBD	--	--	TBD
Tape and Tabulations	--	--	--	--	TBD	--	--	TBD
Staff Years	--	--	--	--	3.5	--	--	3.5
$ Amount	--	--	--	--	$110,000	--	--	$115,000

SOI Studies of Tax Exempt Organizations: Measures of Population, Sample, Completion Dates, and Cost Estimates by Tax Year continued

	1985	1986	1987	1988	1989	1990	1991	1992
Farmers' Cooperatives (Form 990C)								
Population	--	--	--	--	6,000	--	--	6,000
Sample	--	--	--	--	6,000	--	--	6,000
Data Capture								
Start	--	--	--	--	TBD	--	--	TBD
Finish	--	--	--	--	TBD	--	--	TBD
Tape and Tabulations	--	--	--	--	TBD	--	--	TBD
Staff Years	--	--	--	--	4.0	--	--	4.0
$ Amount	--	--	--	--	$125,000	--	--	$135,000

[1] 501(c)(3) Organizations only; 1986 will have redistributed sample to obtain a better representation of social welfare organizations.

[2] Includes all subsection codes

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THE FUTURE WORLD OF WORK:
IMPACT ON THE INDEPENDENT SECTOR

by

Linda J. Forbes, Director
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Prepared for the 1988 Spring Research Forum
"Looking Forward to the Year 2000:
Public Policy and Philanthropy"

San Francisco, California
March 17-18, 1988

Introduction

Since 1980, United Way of America has conducted a formal process of monitoring changes in environmental trends and events. A volunteer committee that includes among its members some of the nation's foremost futurists and issues managers[1] supports this process, which is referred to as environmental scanning.[2] The intent of environmental scanning and resultant publications[3] is to assist United Way of America and United Ways around the country to strategically manage their organizations.[4]

During 1987, the United Way of America Environmental Scan Committee identified events and trends related to the world of work which they felt would have an impact on United Way organizations. This paper reports the results of this identification and of a survey that ranked these trends and events in order of importance. It also presents some information about the top-ranking trends and speculates on the impact of issues suggested by these trends on the independent sector. During 1988, United Way of America will publish The Future World of Work II,[5] a full report of the issues and their implications for nonprofits.

Issues Identification Process

The United Way of America Environmental Scan Committee meets twice a year, in April and in October. At its April, 1987 meeting, the committee identified 43 work-related environmental trends and events that will be important for United Ways.[6] These trends and events were put into a questionnaire that was distributed to committee members (total membership is 36). Members ranked each trend on (1) **probability** of development into a major issue for United Way, (2) **impact** on United Way, should the trend or event become a major issue, and (3) **time frame** for each issue to mature sufficiently to require significant resources for its management. Probability and impact rankings were on a scale from 0 (highly improbable, negligible impact) to 10 (highly probable, major structural change). Time frame rankings were: 0 - issue passed; 1 -near term (1987-88); 2 - medium term (1989-91); and 3- long term (1992-1996).

Thirty committee members responded to the questionnaire. Responses were analyzed using Delphi Decision Support System software developed by the Policy Analysis Company, Inc.[7] This software ranks responses on frequency, degree of consensus among respondents, and respondent confidence in response. Since respondents were not asked to rate the degree of confidence with which they made their predictions, the analysis for this study involved only the first two rankings, frequency and consensus.

Two trends ranked highest on this questionnaire on both probability and impact. These were:

Rank 1: Increasing growth and greater workplace impact of family and personal concerns, such as drugs, alcohol, smoking, stress, and care of family members (children and elderly).

Rank 1: Greater proportion of workforce employed in small and medium-sized businesses.

Personal concerns ranked slightly higher on probability of development into a major issue for United Way, while more employment in smaller businesses ranked slightly higher on impact. Respondents saw both of these trends maturing late in 1988. The scores for respondent consensus were very high on these items. The personal concerns item had the highest consensus score of any trend listed. This means that committee members were in strong agreement on the ranking they assigned to this item. Its score was not an outcome of averaging extreme scores.

Other high ranking trends were:

Rank 3: Growing impact of corporate restructuring.

Rank 4: Growing importance of the international marketplace.

Rank 5: More corporate downsizing and more outsourcing, including hiring released staff back as contractors.

Rank 6: More automation/robotization/computerization of the workplace; greater impact of technology on the clerical workforce.

Rank 7: Growing importance of job retraining.

Rank 8: Growth in the offshore workforce, including service workers. More U.S. corporate "shells" with production offshore but with marketing here.

Rank 9: Greater use of previously "underutilized" groups in the workforce; i.e., handicapped, minorities, women.

Rank 9: Growing impact/conflict of work and home demands among both men and women, including stress syndrome among "superwomen" and single-parent fathers.

Rank 11: More foreign ownership and introduction of foreign management practices and values to the U.S. workforce.

Rank 11: More immigrants in the workforce.

Rank 13: Declining corporate loyalty among workers.

Rank 14: Growing impact of communication networks.

Trends listed on the questionnaire that respondents assigned their lowest probability and impact scores were "Re-emergence of unions as a powerful force, especially among white-collar workers," and "Increase of terrorism, especially aimed at companies supporting the national infrastructure (telephone, gas, water, electric)."

Estimated time frames for issue maturity on trends ranking 3 to 14 ranged from near-term (1987) for "Growing impact of corporate restructuring" to medium-term -- around 1990 -- for "More foreign ownership and introduction of foreign management practices and values," and for "More automation/robotization/ computerization." Respondents saw most of the listed trends as maturing in the near- or medium-term. Trends assigned the most distant maturity were "Growth of cottage industries and attendant legal and insurance-related concerns," and "More postponed retirements."

Consensus on probability of trends ranked 3 to 14 was strongest on "Growing impact of corporate restructuring" and "Growing importance of the international marketplace." It was weakest on "Growth in offshore workforce" and "Declining corporate loyalty." Consensus on impact of each trend on United Way was strongest on "More corporate downsizing and more outsourcing" and weakest on "Growing importance of job retraining," "More foreign ownership," and "Growing impact of communication networks."

The Environmental Scan Committee reviewed these survey results at its October, 1987 meeting. It also reviewed preliminary reports on these trends drafted by United Way of America staff. Based on committee discussion and recommendations, the committee combined these trends and events into eight broad "world of work" issues that they regard as important for United Way's future. These issues are:

- Family and Personal Concerns
- Underutilized Groups
- Education, Training, and Retraining
- Corporate Restructuring
- Small Business
- International Marketplace
- Automation/Robotization/Computerization
- Employment Prospects

During their discussion, committee members noted that along with these issues, there are some other trends that bear watching because of their growing impact on the world of work. These trends concern AIDS, the right to privacy, the medically indigent, employment of the elderly, and emergence of a two-tier workforce (highly skilled professionals and unskilled support workers).

Future World of Work Issues for the Independent Sector

The eight "world of work" issues identified by the United Way of America Environmental Scan Committee are important not only for United Ways. They will have significant implications for all business organizations, regardless of sector. They are discussed here, however, primarily in the context of their impact on the independent sector.

1. **Family and Personal Concerns:** Personal and family issues are increasingly affecting the workplace.

Problems and concerns in the personal lives of Americans are spilling over into the workplace. More than ever, people must balance their work lives with competing demands of dependent care (of both children and elderly relatives) and of time needed for personal chores and leisure activity. One outcome of this pressure of competing demands is stress, and symptoms of stress are apparent in the workplace, where smoking, alcohol and drug abuse, and lack of physical exercise affect employee productivity.

Because the primary function of institutions in the independent sector is to respond in one form or other to personal needs, concerns, and problems, the impact of this issue on need for the sector's services is apparent. Services will be required to help working people care for their children and their aged relatives, to reduce stress through recreational activity, and to overcome personally destructive symptoms of stress such as smoking and substance abuse. Workers will need counseling to help them manage the demands on their time and to accept the limits of what they can accomplish. Many of these needs are not new. What is new is the opportunity to work with for-profit businesses to provide services for workers. Voluntary organizations may provide some services at the workplace. In other instances, businesses may purchase off-site services for their workers. Businesses increasingly recognize how personal concerns affect worker productivity. Many business firms are eager for linkages with independent sector agencies that provide services. One example of this need is the rapid growth of Employee Assistance Programs (EAPs). More than 10,000 American companies have EAPs, including 80 percent of Fortune 500 firms.[8]

While this issue presents opportunity for service provision, it also means that the independent sector workforce will be similarly impacted by personal problems and concerns. Independent sector employers will have to become more attuned and responsive to needs among their own employees for assistance with child and elder care, and for stress-reducing and rehabilitative programs. Employers are able to offer some assistance through employee benefits programs. Employees will increasingly want cafeteria-style benefit plans where, for example, they may substitute elder- care for child-care benefits, or where they may choose from among a number of health-care options.

This issue also has implications for the voluntary workforce on which many independent sector organizations rely. When time pressures mount, people have less time for volunteer activity. For organizations, this may mean structuring new, less time-intensive roles for volunteers, or changing hours of meetings and other activities to suit volunteer needs.

Some of these personal concerns involve social policy issues that are appropriate for independent sector response. These include policies related to child care and care of the elderly (including long-term care and issues associated with medical care costs). There are also issues related to how firms handle substance-abusing employees, including the use of drug screening tests and policies on smoking at the workplace.

2. **Underutilized Groups:** There will continue to be greater employment of previously "underutilized" segments of the population; specifically, women, minorities, and the disabled.

Between now and the year 2000, the American workforce will grow at a slower rate than it has at any time since the Great Depression. During this period, over ninety percent of workforce entrants will be women, minority group members, or immigrants.[9] Previously "underutilized," these groups, as well as the disabled, will find new work opportunities as the availability of "traditional" entrants, white males, declines.

Women, in the year 2000, will be 47 percent of the workforce, up from 42.5 percent in 1980. Most will still be concentrated in "women's work" -- jobs comprised of over 90 percent women and generally paying less than men's jobs.[10] Greater female workforce participation is affecting and will continue to affect all economic sectors. Along with employer-sponsored child care programs, women will look for more part-time jobs, flexible hours, and stay-at-home jobs. Interest in these options relates to the desire to spend more time with children. Only half of working mothers believe they can adequately fulfill their responsibilities to their children if they work full time.[11] Independent sector organizations will continue to have a significant role in providing services that help women to find and to remain in suitable jobs. Skills that earn more than a minimum wage are vital for women who support families. Training, placement, and advocacy services for women will remain in demand. Other implications of women's workforce participation will be persistence of pay equity issues, a continued push by women for higher-level positions in organizations, and, according to some observers, development of new "female" managerial styles. To a large extent, independent sector organizations have already adjusted to a major impact of greater female workforce participation -- the significantly diminished availability of housewives as daytime volunteers.

Among minorities, Hispanics will have the fastest labor force growth, followed by blacks, and then Asians and other races.[12] Geographic and educational imbalances will continue to limit opportunities for some minorities. Many live in declining central cities and are employed in slower-growing occupations. One government study found that blacks and Hispanics are 35 percent more likely to be employed in occupations projected by the Bureau of Labor Statistics to lose the greatest number of jobs between 1978 and 1990.[13] Many minorities in the workforce will also be new immigrants to this country. One impact of this issue on the voluntary sector will be continuing demand from minorities (and the disabled) for employment-related services and job training. Equal employment opportunity issues will persist, and, like women, minorities will seek and will earn higher positions in independent sector organizations. This greater workforce participation of women and minorities also has implications for organizations that raise funds at the workplace. Responsiveness to the needs and interests of women and minorities will be important factors in workplace fund solicitation.

3. **Education, Training, and Retraining:** Worker education, training, and retraining are an increasingly significant part of meeting the challenge of a rapidly-changing, technologically-advanced economy.

For Americans, education for employment is more and more a lifelong process. With changes in the economy and technological advances rapidly altering the nature of many jobs, a typical worker may have five or six different jobs and three to four different occupations in a lifetime.[14] This means a need for ongoing training for increasingly complex jobs, and this need is emerging at a time when Americans are questioning the fundamental capacities of their educational institutions. New jobs are requiring high skill levels and creative thinking. Yet a 1985 survey by the Committee for Economic Development found that many schools are failing to develop these skills, particularly among young people who are poor, disadvantaged, and minority.[15] Most institutions of higher learning have remedial programs, and businesses invested $25 billion in 1985 alone to teach employees remedial reading, writing, and mathematics.[16]

For the independent sector, this is a major issue of public policy. Is the public education system failing? If so, how must the independent sector respond? Workforce growth is slowing, which means that a greater proportion of American workers must be equipped with high-level technical skills. Most new jobs created between now and the end of the century will require at least some college education.[17] If this nation cannot adequately equip enough young people, will this mean encouraging immigration of well-educated foreigners? What is the role of business as educator and how far do business responsibilities for education extend? The Carnegie Foundation suggests that even now the corporate education system to train and retrain workers rivals the public educational system in this nation.[18] As businesses earmark greater proportions of their voluntary contributions to support educational programs, how will this impact corporate support for other sector services? What services should the independent sector directly provide? Should it provide, for example, programs to combat illiteracy? And, finally, what will be the ongoing training needs of independent sector employees?

4. **Corporate Restructuring:** The corporate atmosphere will remain turbulent for the remainder of the 1980s and during the 1990s.

Corporate restructuring has touched almost every major American corporation. Since 1980, Fortune 500 firms have laid off 2.8 million workers due to various forms of corporate restructuring.[19] Mergers and acquisitions, downsizing, adding new technologies, streamlining management, and reorganizing to compete with foreign firms have dramatically altered the corporate landscape, and will continue to do so. Financial failures during the 1987 stock market crash may dampen enthusiasm for mergers and acquisitions brought about for short-term financial gain, but other factors will sustain this activity. For instance, companies will continue to use mergers and acquisitions to gain needed capabilities in areas such as data processing, research, marketing, and communications. Other forms of restructuring -- relocations, plant closings, sales to other companies, and automation-induced reorganizations will continue to reshape the American corporation.

This corporate turbulence has had and will continue to have a significant impact on American workers. For many workers, restructuring means early retirement, layoffs, or outright firings. Around 11.5 million workers lost their jobs in restructurings between 1979 and 1984. Many of these workers were also left without pension and health insurance benefits.[20]

For the independent sector, corporate restructuring may create demand for human services from people whose lives are affected by job loss. These services may range from an early retiree's desire for a new volunteer opportunity to a family's need for housing because it no longer able to keep up rent or mortgage payments. Blue-collar workers are often especially hard-hit when plants close. They may find themselves without marketable skills and forced to take jobs paying far less than their old salaries. Corporate restructuring may also have a negative effect on corporate philanthropic activities. Merger of two companies with corporate contributions budgets generally means a reduction in the total corporate contribution. Moreover, the need to put a new corporation together can make executives less willing to conduct a workplace solicitation or to entertain new requests for solicitation. Site closings and massive layoffs will also injure philanthropic organizations relying upon employees for contributions and volunteer activity.

5. **Small Business:** The ongoing dynamic growth in small businesses will continue to alter traditional employment patterns and ways of doing business.

Today, small businesses, or firms with fewer than 100 workers, are responsible for two-thirds of the Gross National Product (GNP).[21] During the 1980s, small businesses have been responsible for nearly two-thirds of the nation's job growth.[22] In 1985 alone, small business starts amounted to 1.4 million. This recent phenomenal growth of small businesses is one outcome of new technologies that do not require large capital investment or rely on large size for productivity. Another factor in small business growth is entrepreneurial spirit, especially among women, who are starting new businesses at five times the rate of men. Despite these factors promoting development of small business, half of new companies close within five years.[23]

While small businesses may be profitable for owners, financial security is frequently shaky for small business employees. Compared to large corporations, salaries in small businesses are often lower, especially when the firm is young and the owner needs to invest in expansion. Also, employee benefits are generally limited. Unlike larger firms, small businesses generally do not offer comprehensive medical plans or benefits such as child care, elder care, and maternity and paternity leave. For organizations raising funds at the workplace, small businesses are a special challenge. To effectively solicit small business owners and employees, philanthropic organizations must devote resources to market research, targeting markets, cultivation, and follow-up. Small business owners, as entrepreneurs, may also present some new values and attitudes to independent sector organizations. While they may not have had exposure to the "corporate citizenship" philosophy of larger and older firms, their interest in and approach to social and community issues may be dynamic and innovative. If harnessed, this entrepreneurial energy may be tremendously beneficial for the community. Independent sector organizations will find that they require new approaches for delivering services to workers at small businesses. To reach these workers, agencies may have to set up fairs in office parks and malls, work through business trade associations, provide information and referral over computer networks, or introduce services via video tapes.

6. **International Marketplace:** The globalization of the international economy will continue to influence American business operations and philanthropy.

America is part of an interdependent global economy which it no longer dominates. U.S. share of world production fell from 35 percent in 1960 to 22 percent in 1980.[24] Foreign investment in the U.S. has grown significantly; in 1987, it amounted to $1.5 trillion.[25] The future of this investment is not certain; with decline in the strength of the dollar, the U.S. is less of a desirable haven for foreign investors. American firms continue to invest abroad, often to take advantage of low foreign labor costs. Movement of American jobs offshore has not only occurred in the manufacturing sector. Foreign workers now do service jobs, such as keypunching, for American firms.

While only two to three percent of American industry is foreign-owned -- and mostly by Britain, followed by Canada and then Japan[26] -- foreign ownership is one aspect of the international economy that has implications for America's independent sector. Foreign owners have had to learn American-style philanthropy, and some are learning very quickly, especially the Japanese. Toyota recently endowed a $10 million foundation, Hitachi a $20 million foundation, and other Japanese firms are following suit.[27] Independent sector organizations must learn how to approach and involve foreign owners in American philanthropic activity.

7. **Automation/Robotization/Computerization:** Automation, computerization, and robotization will spread more quickly through the workplace, changing both the nature of work and what it takes to be successful in the marketplace.

Automation, or the use of machines to replace man's physical or mental labor, will accelerate for the remainder of the century. American business is developing and applying new technologies (computers, robotics, telecommunications, artificial intelligence) in an effort to succeed in the competitive global marketplace.

Use of new technologies to expand services and improve products will continue to be important for independent sector organizations. Computers will penetrate their workplaces, where they will be used for information gathering, storage, analysis, and dissemination, as well as for word processing and other applications. Communication networks will link people for fast, non-hierarchical idea generation and decision making. It is now possible to communicate with large numbers of co-workers with the push of a single button. Within a community, advocacy groups may organize through a communications network rather than through public meetings. For independent sector agencies, another technological application is use of electronic funds transfer for contributions collection.

8. **Employment Prospects:** The rapidly changing economy will create an unstable employment picture for most workers.

Overall employment growth is slowing; however, more than 21 million new jobs will develop in the U.S. economy by the end of the century -- mostly in the service sector.[28] Prospects for jobs in professional, technical, and sales occupations will outstrip opportunities in other fields. Goods-producing (including manufacturing) jobs will experience almost no change in employment levels from now through 2000. In the services sector, an expansion of 20 million new jobs by 2000 will be driven by growth in health care, businesses services, and wholesale and retail trade.[29] However, for many Americans, employment prospects are not good. While unemployment is currently low, millions of Americans in their prime working years are still outside of the workforce. America's jobless include not only the unemployed, but also those who have given up looking for work and those who work part-time but would like full-time jobs. Many of these jobless are among the nation's more than 20 million citizens living in poverty.

Challenges for the independent sector related to these employment prospects include development of systems to match people with the education and training they need to survive in a changing work world. This includes assistance to underemployed, unemployed, and displaced workers. For workers who cannot find suitable jobs but who want to keep active, availability of volunteer opportunities may be a vital and important link to the workplace. Voluntary agencies must also monitor and plan for their own changing employment needs. As workforce growth slows and skill requirements increase, some fields, such as health care, may be hit by labor shortages.

NOTES

[1] The committee membership roster is available from United Way of America Strategic Planning and Market Research Division, 701 N. Fairfax Street, Alexandria, Va., 22314.

[2] Environmental scanning as used in this context refers to both monitoring trends and events that have already been identified and to detecting signals (frequently weak) of new trend and events.

[3] Including What Lies Ahead, a biennial national environmental scan and periodic Trend Intelligence Program publications on special issues.

[4] Environmental Analysis, or gathering information about environmental trends and events and speculating about their impact on the organization is one of two data-gathering steps (the other is Organizational Assessment) of a six-step strategic management process model. This model is described in United Way of America's seven-booklet Strategic Management and United Way series.

[5] The first edition of Future World of Work was published by United Way of America in 1981.

[6] Complete listing available from United Way of America, address under note (1).

[7] Policy Analysis Company, Inc., is located at 1090 Vermont Avenue, N.W., #927, Washington, D.C. 20005

[8] "Addicted Worker Problem Leads to New Growth Industry," John Naisbitt's Trend Letter, May 14, 1987, p. 6.

[9] U.S. Dept. of Labor, "Projections 2000: Summary," (Bureau of Labor Statistics News Release, June 25, 1987), p. 1.

[10] Hudson Institute. Workforce 2000: Work and Workers for the 21st Century (Indianapolis: Hudson Institute, Inc., 1987), p. 85.

[11] Hudson Institute, p. 86.

[12] U.S. Dept. of Labor, p. 1.

[13] Hudson Institute, p. 91.

[14] "U.S. Should Prepare Now for Massive Retraining," What's Next, Spring, 1985.

[15] "Illiteracy is a Major Business Problem," Washington Times, March 3, 1987.

[16] National Commission for Employment Policy, Basic Skills and Employment Training Programs: Can the Combination

Benefit Employers, Youth and Community Institutions? (June, 1987), p. 1.

[17] U.S. Dept. of Labor, p. 4

[18] United Way of America. What Lies Ahead: Looking Toward the '90s (Alexandria, Va.: United Way of America, 1987), p. 28.

[19] David L. Birch, Job Creation in America (New York: The Free Press, 1987), p. 120.

[20] U.S. Office of Technology Assessment, Technology and Structural Unemployment: Re-employing Displaced Adults (January, 1986), p. 3, 8-9.

[21] University of Notre Dame Small Business and Private Enterprise Committee, Small Business is Big Business (Brochure, not dated).

[22] "The Rise and Fall of Everybody," Inc., September, 1987, p. 18.

[23] University of Notre Dame Small Business and Private Enterprise Committee.

[24] Reich, Robert. Tales of a New America (New York: Times Books, 1987), p. 44.

[25] U.S. Joint Economic Committee, Trade Deficits, Foreign Debt, and Sagging Growth (September, 1986).

[26] U.S. Dept. of Commerce, Bureau of Economic Analysis, Survey of Current Business, vol. 67 (August, 1987).

[27] "Japanese Charity Begins in USA.," USA Today, October 1, 1987, p. 2B.

[28] U.S. Dept. of Labor, p. 3.

[29] U.S. Dept. of Labor, Bureau of Labor Statistics, "Projections 2000," Monthly Labor Review, September, 1987, p. 37.

SECTION SEVEN:

PHILANTHROPY, PUBLIC POLICY AND THE POOR

Corporate Social Responsibility, Public Policy and Poverty

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CORPORATE SOCIAL RESPONSIBILITY, PUBLIC POLICY AND POVERTY

by

Peter Goldberg
Vice President, Public Responsibility
Primerica Corporation
and
Vice President, Primerica Foundation

Prepared for the 1988 Spring Research Forum
"Looking Forward to the Year 2000:
Public Policy and Philanthropy"

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1. OVERVIEW

The philosophic underpinnings of this paper are straightforward and unambiguous. Our is a society of interdependent institutions. The business community -- one major institution in American society -- is not an impregnable island unto itself. Whether we like it or not, the business community has a long term stake in how this nation addresses the major social issues of our time. Poverty in America stands out as a major social issue of the 1980s. Nonetheless, despite substantial increases in corporate philanthropy and the advent of public-private partnerships, it is still unclear just how committed corporations are to anti-poverty efforts and just how seriously they view the problems of poverty in American society. National efforts to alleviate the tragedy of poverty in the richest nation in the world would be considerably strengthened if the business community would voice more active public policy support for governmentally financed anti-poverty programs.

2. THE EXTENT OF POVERTY AND THE GROWING GAP IN INCOME DISTRIBUTION

Although there are many different interpretations about the nature of poverty in America and prescriptions about how to respond, the size of the problem is large by anyone's definition. Poverty in America is a major social concern. The business community has a vital long term interest in the poverty problem. Poor people have less money with which to buy the products businesses make and the services they offer; poor people need greater levels of public assistance, which in turn means higher tax rates. Poor children, poorly educated, grow up poorly prepared to participate in the labor force. Given current demographics, business may find itself unable to hire all the workers it needs if too many Americans grow up lacking basic skills, or at least will face unnecessarily high training costs. Finally, the increasing number of people entrenched deep in poverty raises the specter of a permanent underclass, a form of social and economic dynamite which is neither in the best interests of the business community nor the larger society.

According to recent Census Bureau data[1], 32.4 million Americans -- 13.6% of the population -- lived below the poverty line in 1986. Moreover, 12.7 million people subsisted on incomes of less than one half the official poverty line. The poverty rate for Black Americans in 1986 was 31.1% and for Hispanics it was 27.3%.

The future health and vitality of the United States rests with its children. Yet in 1986, 20.5% of all American children lived in conditions of poverty. Among Black children the rate was 43%, and the childhood poverty rate for Hispanic children was 27.3%.

Poverty is commonly associated with many indices of children, youth and family problems, such as child abuse, juvenile delinquency, infant mortality and drug abuse. The social and economic costs of poverty related problems ripple throughout our society, impacting just about every individual and institution in one way or another.

The national poverty rate has declined very slightly in each of the past two years. Whatever comfort may be derived from this trend, however, is not necessarily shared by those who work closer to the front lines. Since 1982, the U.S. Conference of Mayors has regularly surveyed the extent of hunger, homelessness and poverty in American cities. Their December, 1987 report paints a bleak picture of sustained and serious social and economic conditions[2].

Compounding the very high rate of poverty in the 1980s are Census Bureau data showing an ever widening gap between rich and poor. According to the Center on Budget and Policy Priorities, in 1986 the wealthiest 20% of American families received 43.7% of the national family income, the highest percentage ever recorded since the Census Bureau began collecting such data in 1947. At the other end of the scale, the poorest 40% of American families received 15.4% of the national family income, the lowest percentage ever recorded[3].

The large and growing number of people living in deep and entrenched poverty in the 1980s raises serious concerns about the creation of a permanent underclass, a group of American citizens for whom the hope of escaping poverty and pursuing the American dream becomes increasingly remote.

The economic and public policies which have exacerbated the dire straits of millions of poor Americans during this decade have been generally more favorable to the business community. Corporate tax rates have gone down. Corporate profits have increased handsomely. The stock market has risen significantly since 1982 (even given the October 1987 "crash") yielding good returns for those who have invested in it.

Public opinion about corporate wealth is molded by other observations as well. The proliferation of high-stakes corporate takeover battles leaves the public uneasy and with a sense that such boardroom drama enriches very few at the expense of many more. Highly publicized insider trading scandals add further fuel to the public's sense that in this era of government deregulation, greed is overwhelming legitimate business accomplishments and the public interest.

The intermixing of widely held impressions with available data shapes a picture of corporate America that stands in sharp contrast to that view of the other America defined by the Census Bureau statistics on poverty. With these pictures in mind we now turn to a discussion of how corporations have reacted and responded to the problems of poverty in the 1980s.

3. CORPORATE PHILANTHROPY AND PUBLIC-PRIVATE PARTNERSHIPS

The adequacy of the corporate response to the problems of poverty in America is subject to different interpretations, dependent upon wholly subjective standards and reference points. It is possible to set low standards which corporations can meet with ease and to great applause. It is also possible to set high standards and watch more critically as corporations approach the challenge with temerity.

From one vantage point it is quite possible to applaud America's corporations for their commitment to philanthropy during the 1980s. Corporate giving to nonprofit organizations rose from $2.4 billion in 1980 to $4.4 billion in 1985[4], although this increase has now apparently leveled out.

From a different vantage point, however, others may suspect that the increases in corporate philanthropy are something of a palliative, of uncertain endurance, with uncertain motives and of limited utility. The skeptic would point out that increases in corporate philanthropy should not be allowed to mask the basic fact that America's corporations benefitted from substantial reductions in tax rates, as well as national public policies, which have, in effect, made the rich richer and the poor poorer.

From one perspective it is quite possible to applaud the corporate commitment to social problem solving through public private partnerships. Encouraged by all levels of government, there are scores of successful examples of corporate participation in problem solving in fields as diverse as hunger, education, housing, and youth employment.

From that other perspective, however, there are those who can point out that the vast majority of America's corporations were woefully silent as the Reagan Administration and the Congress trimmed away the so-called "social safety net." From this perspective, corporate philanthropy and participation in public private partnerships would not have been so important had the federal government not been allowed to redefine and reduce its commitments to domestic anti-poverty programs.

In one sense though, American corporations have exceeded their social and public responsibilities because, in point of fact, they are not legally compelled to make any philanthropic contributions at all. Corporations do not have to participate in any public private partnerships whatsoever. But corporations have chosen voluntarily to be involved. The motivations for this involvement may be fueled by different mixtures of altruism and self interest. Whether these commitments are of the here-today-and-gone-tomorrow variety or are of more lasting endurance also varies from one company to the next. Regardless, corporations have frequently sought recognition and been widely hailed for their generous willingness to participate in social problem solving. It is neither unreasonable nor unfair to set high standards by which to appraise the aggregate effectiveness of such efforts.

High standards of expectation are also preferable to low standards because (1) the needs of people in poverty are substantial, and (2) corporations have a long term, important stake in how American society addresses the problems of poverty. It is also healthier to search for challenges which extend our efforts and to find ways to improve upon them than it is to engage in hearty rounds of back-slapping and self-congratulation.

4. THE LIMITS OF CORPORATE PHILANTHROPY

Despite the impressive growth of corporate philanthropy in the 1980s, the overall dollar value of corporate grantmaking could hardly make a dent in the constellation of poverty related problems. The Salamon-Abramson analysis of Nonprofit Organizations and the FY 1988 budget makes clear just how difficult it is for all private giving to offset federal spending reductions[5]. It is certainly not unreasonable -- indeed it is probably very conservative -- to suggest that we could double, double, and double again the amount of corporate philanthropic giving and it would still be inadequate to meet the needs of poor Americans and still be small in total dollar size compared to a relatively small percentage increase in government commitments.

Moreover, only a fraction of the corporate philanthropic budget is directed towards poverty problems. Corporate foundations make grants to a diversity of organizations for a diversity of reasons. Poverty is not at the head of the priority list for most corporate foundations. While the overall amount of corporate philanthropic funding available for serious antipoverty efforts has never been precisely calculated, it is most assuredly well under one billion dollars per year. The actual impact of even this amount is further diluted by legitimate concerns about the general thoughtfulness and quality of effort which characterize even well-intentioned corporate grantmaking[6].

Another factor which limits the effectiveness of corporate philanthropy in addressing problems of poverty is that corporate grantmaking tends not to be countercyclical. Poverty problems worsen during recessions and the need for assistance increases. However, recessions require many corporate grantmakers to tighten their own belts. This belt tightening is precipitated because the budgets of many corporate foundations are indexed against pre-tax income levels. In recessions pre-tax income does not rise at the same rate as in periods of growth, and corporate expenses of all types are scrutinized more carefully. Ironically, just when corporate grantmaking could be most valuable in addressing the increased needs of growing numbers of poor people, corporate grantmakers must hunker down with the rest of corporate America to weather the storms of economic recession.

This scenario could be particularly profound whenever the next recession occurs. In recessions, unemployment and poverty levels are likely to rise, with the increase somewhat correlated to the severity and duration of the recession. Since the last recession in 1981-82, unemployment levels have dropped considerably, but the poverty rate remains abnormally high. Thus it is possible that the next recession - whatever its overall severity - could hurt poor people disproportionately.

5. THE LIMITS OF PUBLIC PRIVATE PARTNERSHIPS

The potential of public private partnerships to alleviate poverty is also limited. Such partnerships can help to identify innovative solutions to some problems; they can become the means by which to offer some assistance to some people and some communities. It is a mistake, however, to let such partnerships be magnified and misinterpreted as a comprehensive form of private sector substitution for public sector responsibility.

Corporate donations of food to the national network of food banks, for example, have risen impressively from a few million pounds in 1979 to 352 million pounds in 1986[7]. These donations - as welcome as they are - are, however, only a stopgap measure and cannot solve the problems of hunger and inadequate nutrition for millions of Americans. A more effective response would be to ensure that all eligible recipients participated in the federal food stamp program and received benefits sufficient to maintain adequate nutritional levels.

School business partnerships are also limited. This type of partnership has become exceedingly popular in the corporate community. Many schools and many school children have benefitted from school business partnerships. The policy problem with focusing on the successful examples of school business partnerships is that they overlook the overwhelming majority of schools and school children not affected by them. In contrast to the corporate commitment to school business partnerships, corporate executives have been far less outspoken in their support of greater public sector expenditures for successful educational programs like Head Start and Chapter One, effective programs which should be made available to all disadvantaged school children.

Public private partnerships have provided corporations and corporate executives with valuable learning experiences. Three lessons stand out. First, these partnerships offer a window to the world in which less fortunate Americans must struggle to survive. Senior corporate executives are often touched by their personal experiences. They see conditions of poverty first-hand.

They witness valiant efforts to escape the traps of poverty. They have renewed appreciation of the value of programs to help poor people. Second, private sector partnership programs with government agencies offer penetrating insights into the extraordinary problems of administering effective, large public sector programs. Corporate executives may emerge from their partnership experiences with equal or even more withering criticisms of the public sector bureaucracy, but they also frequently gain a new appreciation of the scope, complexity and difficulty of running large public sector programs. Finally, corporate sector leaders have to be impressed by the limits of the private sector to respond to the overwhelming size of poverty related problems without the involvement of the public sector. It far exceeds anyone's definition of corporate social responsibility to try to replicate successful public private partnership programs at a sustained year-to-year level sufficient to respond to intransigent social problems of a large magnitude.

6. THE NEED FOR CORPORATE PARTICIPATION IN THE PUBLIC POLICY MAKING PROCESS

Should corporate America be satisfied with its anti-poverty efforts solely through its own philanthropy and participation in public private partnerships without also speaking up in vigorous support of effective public sector programs, particularly underfunded government programs with demonstrated track records of success? Is corporate America so enamored with its own efforts that it has forgotten to look at the problems which prompted those efforts in the first place? Will corporate America continue to be preoccupied with private sector initiatives which are limited in potential? Or, are these efforts the necessary passageway through which most corporate executives must travel before they discover the larger anti-poverty resources potentially available through the public sector?

A breakthrough of sorts occurred in March 1986 when five senior executives from five different major American businesses testified together at a joint House-Senate hearing on behalf of the reauthorization of federal aid to public elementary and secondary schools serving high concentrations of disadvantaged children[8]. It was the first time in the twenty year history of the Chapter One program (formerly known as Title One) that any American businessmen have directly communicated their concern and support to Congress for this important anti-poverty and education program. The program's long time champion, Congressman Augustus Hawkins referred to the businessmen's testimony as an important element in the recent reauthorization process[9]. The additional funds now authorized for this federal program will exceed the annual dollar value of all school business partnerships nationwide.

In another example of the willingness of the business community to involve itself in the education public policy making process, the Committee for Economic Development recently issued a report expressing strong support for the federal government's Head Start program[10]. However, these examples stand in relative isolation and thus far are confined primarily to issues of public education. There has been very little outspoken corporate support for most public sector anti-poverty efforts.

In 1985, Fred Hechinger of the New York Times issued a stern warning about possible corporate duplicity with respect to its support for public education. Hechinger wrote in the Harvard Business Review "...in the end, all these cooperative ventures [school-business partnerships] will amount to little more than public relations unless the business community abandons its frequently schizophrenic posture; supporting the local schools while simultaneously instructing, or at least permitting, its lobbyists to support cuts in state and federal expenditures for public education and such legislation as tax credits for parents whose children attend private schools. Common sense should show the futility of any corporate policy that gives to the local schools with one hand and yet takes away funds with the other[11]." Hechinger's words can be applied to a broader range of corporate involvement in the pressing social problems of the day.

Not every governmentally funded anti-poverty program is an unqualified success; nor is every one an abject failure. Corporations and corporate executives ought to be both encouraged and prodded to speak out on behalf of effective programs such as Head Start, WIC, and Child Immunization; they ought to lend their talents and energies to help strengthen marginally effective programs. And business leaders ought to participate in the development of new public policies and programs to attack poverty in America. After all, public policy and the priorities expressed through government budget-making will be significant determinants of the nature, extent and severity of poverty in America.

7. WHAT DOES THE FUTURE HOLD?

For those who set high standards of expectation for corporate contributions to national anti-poverty efforts, the aggregate effectiveness of current programs falls short of the mark. Disappointment may conceivably be tempered by belief in progress -- such as growing sophistication of partnership and philanthropic efforts and occasional glimmers of hope that some corporations and corporate executives are willing to speak out forcefully, even passionately, on the important social and economic public policy decisions that affect poverty in the United States.

But beyond the fact that this progress is not fast enough to produce any measurable dent in poverty, business may be on the way to paying a price in the public's perceptions of it.

According to a recent issue of Time Magazine for example, "If Big Government was the villain of the Reagan cycle of American history, the bete noire of the new may be Big Business[12]." Time goes on to cite surveys from pollster Lou Harris which showed 69 percent of the American public giving corporate America a favorable rating in 1979. The comparable 1986 Harris figure was 35 percent. Harris concludes that "...the mood about business has turned negative on a massive scale[13]."

What will happen to the corporate commitment to philanthropy and public private partnerships if Harris is right? Will business undertake to do more about poverty in order to redeem itself in the public's eye? Or, will the corporate sector display less sensitivity to poverty in America when government is regulating them more and applauding them less? What will happen to the corporate commitment to corporate philanthropy and social responsibility if corporate tax rates go up?

In many ways these are litmus type questions for the corporate community. The answers will shed much light on what corporate America believes about poverty; whether corporate efforts to address poverty problems are short-term, paper thin and of questionable motivation, or whether they are the modest beginnings of a longer term commitment; whether corporate America believes that the problems of poverty affect their long-term health and vitality or whether corporations hold to the "impregnable island" concept.

The answers to these questions are also important to many poor citizens. It is possible to make substantial inroads against poverty without active corporate support in the public policy making and government budget setting processes. These inroads, however, could be made more swiftly, more effectively and deeper if the business community moves into an active and visible advocacy posture.

8. CONCLUSION

In the final analysis, the adequacy of the corporate response to poverty in America depends on the measures one chooses to employ. Measured against themselves over time, corporate philanthropy and public private partnerships have grown in size and sophistication. In a social vacuum, blind to the problems against which they are applied, it is relatively easy to construct an argument of great praise. But if we look at the impact of current efforts upon the problems to which they are directed, the aggregate effectiveness and success and the speed of progress are discouragingly small.

NOTES

[1] For a good discussion of the Census Bureau data see report by the Center on Budget and Policy Priorities, "Gap between Rich and Poor Widest Ever Recorded," 1987.

[2] Reyes and Waxman, 1987.

[3] Center on Budget and Policy Priorities, 1987.

[4] Platzer, 1987.

[5] Salamon and Abramson, 1987.

[6] In an analysis done by O'Connell, he estimated that corporate foundations were staffed at almost one-half the level of private foundations on a grant dollar basis. See O'Connell, 1987.

[7] Second Harvest, 1987.

[8] Woodside _et al_., 1987.

[9] New York Times, October 26, 1987.

[10] Committee for Economic Development, 1987.

[11] Hechinger, 1985.

[12] Morrow, 1987.

[13] Morrow, 1987.

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WORKING DRAFT

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THE RESPONSIBILITY OF NONPROFIT HUMAN SERVICE ORGANIZATIONS TOWARDS THE POOR: PRACTICE AND PROSPECTS

by

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The data reported in this paper was collected as part of The Urban Institute's Nonprofit Sector Project. The arguments I present in this paper are mine and do not necessarily reflect the position of The Urban Institute, the funders of the Nonprofit Sector Project, or the Chicago Advisory Committee for the Project.

INTRODUCTION

The official designation of tax-exempt donations as charitable contributions implies that donations to nonprofit human service organizations[1] aid the needy. Newspaper articles also link them to low income clients,[2] many promote their service to the poor and solicit private donations on this basis.[3] An active responsibility for the poor, then, constitutes an important source of legitimacy for nonprofits and few openly discount it.[4] Public policy makers, especially in the Reagan Administration, have also pointed to the role that nonprofits play or should play in maintaining the social safety net for the poor on the assumption that nonprofit and government intervention may substitute for one another.[5]

My findings point to the limits of these assumptions and of existing macroeconomic explanations for the "third sector," which see the nonprofit sector as solving the problem of contract (or market) failure of for-profit firms to insure quality over private monetary gain and the failure of government to provide a sufficient level of services,[6] problems most critical for the low income population. I show, however, that a minority of nonprofit human service organizations serve the poor, even when those least likely to do so are excluded.[7] I conclude that nonprofits face severe external constraints on their ability to independently assist the poor and that their own internal organization and culture do not obviously direct them to this objective.

COMMUNITIES AND NONPROFIT ORGANIZATIONS: INTERLOCKING ECOLOGICAL SYSTEMS

To explain these findings I rely on theoretical perspectives from the community and organizational fields because they provide useful models for understanding organizational behavior. Human ecology views nonprofits as specialized adaptive mechanisms (along with government and economic organizations) through which populations come to grips with their environment and technology.[8] The organizational literature sees nonprofits, like their public and private counterparts, as influenced by their organizational environment and subject to organizational imperatives and institutional practices.[9] Both theoretical perspectives seem essential to explain my findings.

I focus on two key questions in this paper: (1) What are the core features of nonprofit human care organizations, what role do they play in meeting community needs, and does the sector devote particular attention to the poor? (2) What factors explain these core features, what processes of adjustment operate among the organizations, and how do they respond to community needs, adjust to resource decisions made elsewhere, or develop alternative modes of commitments? My approach explicitly assumes that it is appropriate to assess nonprofit effectiveness in meeting the needs of the poor, although individual nonprofits may reject that goal. All organizations are subject to a variety of external standards of effectiveness[10] and standards of anti-poverty effectiveness reflect existing policy concerns about the role of nonprofits in addressing the needs of the poor as well as public conceptions of the meaning of charity and philanthropy.

The last several years have provided a unique opportunity to examine these issues. Significant increases in poverty and service needs (community changes) have occurred.[11] The public sector has reduced its efforts to provide for those needs (resource changes). At the same time, the nonprofit sector operates under a set of institutionalized expectations about appropriate goals, service models, and modes of operations and action. Nonprofits, then, are caught between declining resources, their own well established institutional procedures, and public demands that range from serving existing clients to new and especially needy ones.

RESEARCH APPROACH

The Chicago region combines a number of important features that make it useful for the type of analysis I undertake here. One the one hand, the region and its nonprofit service providers have some features which make it "typical:" Public spending, although low for a large metropolitan area, falls at about the median among the 16 sites included in a recent Urban Institute study and does not deviate markedly from these sites in sources of funding.[12] The size, age, client and service mix of Chicago nonprofits are similar to the composite drawn from these sites.[13]

On the other hand, Chicago nonprofits have faced some circumstances that differ from these other sites. The region has experienced a series of economic setbacks over an extended period, only worsened by the recession of the 1980s. The economic base of the region is changing both in composition and location and the problem of matching jobs with employees is formidable. As a result, substantial portions of the city's low income population face major problems in meeting basic subsistence needs,[14] while public spending on human care declined more than in the other Urban Institute sites during the early 1980s.[15]

Sources of Data

The Urban Institute's Nonprofit Sector project included two waves of mail surveys of nonprofit human service organizations and focused on services, client characteristics, and sources of revenue. A third wave of personal interviews with executive directors was limited to a subset of the surveyed agencies[16] and focused on how nonprofits modify their missions, restructure their programs, and relate to low income or minority clients. The first wave (1982) surveyed 1,008 nonprofits in the Chicago metropolitan area, a 28 percent random sample.[17] Of the 419 nonprofits which responded to the first wave, 300 completed the follow-up survey in late 1984 and a subset of these (128) were interviewed in 1985. This paper uses responses from those 76 nonprofits which provided complete information on sources of revenue and participated in all three waves of data collection.

NONPROFIT ORIENTATION TOWARDS THE POOR

Measuring the extent of poverty focus among nonprofits is not a simple matter. I employed several different approaches. To measure the sustained commitment, or core orientation,[18] of nonprofits to the poor, we asked the executive directors to identify the organization's most important target group and then indicate the extent to which this primary target group was low income. We gave the directors free choice in defining what they meant by low income and in characterizing the target group as entirely, partly or not low income. As shown in the top panel of Table 1, less than one-quarter of the organizations reported that their primary target group was entirely low income, although two-thirds reported it included at least some low income persons. Nevertheless, one-third said it did not.

<< Table 1 about here>>

A somewhat different approach examines the extent to which the directors identify a major link between the service needs of the organization's clients and low income. We asked the directors to identify the major problems of the target group and then followed that with a probe of whether they thought those problems were directly or indirectly related to poverty. The second panel in Table 1 shows the results. Almost half (48 percent) saw no particular relationship between the major problems of their target group and poverty, only 18 percent said there was a strong and direct link.

To look more closely at the extent to which the directors identified two priority problems for the poor, basic needs and employment, as the primary problem of their target group, or endorsed a more traditional social service intervention model to help the poor, I combined the responses from the questions about the most important needs of the primary target group and the perceived link between these problems and poverty. The results are shown in the third panel of Table 1 and are similar to those of panel two.

Finally, I used a straightforward outcome measure of poverty orientation: the percent of clients that are poor as reported in the 1982 and 1985 waves of data collection (see panels four and five in Table 1).[19] These measures reflect more peripheral commitments, because organizations should find it easier to change the type of clients they serve than their core orientations, such as primary target group or major service strategy. The fourth and fifth panel in Table 1 show the results of that analysis. Again, a relatively small proportion of agencies report extensive contacts with low income clients.

The client data, however, should be interpreted with extreme caution. Not all nonprofits have clients (15 percent did not) and client data appear highly unreliable. I compared responses to questions about the numbers of clients served and their characteristics as reported in 1982 and 1985, and reports of shifts in client focus asked in 1984. More than one third of the organizations had major inconsistencies in basic client data.[20] This suggests that information on the number and characteristics of clients is not of sufficiently central focus to the nonprofit sector for it to have developed systematic reporting practices.[21]

Although my measures of organizational goals have obvious shortcomings, they are probably superior to more traditional approaches which derive goals from annual reports, infer them from formal auspices, or rely on the willingness of chief executive officers to articulate them. I included all five indicators of poverty focus in my analysis. As Table 2 shows, the measures are fairly closely related to one another, but they are not identical.

<<Table 2 About Here>>

These patterns of relatively little concern with the poor or their problems become somewhat less important if nonprofits moved notably towards greater focus on them during the early 1980s when the recession and public spending cuts created the most serious problems for the poor. If nonprofits with extensive poverty focus were most able and willing to extend themselves further to the poor then the relationship between existing poverty focus and increasing poverty focus should be high and positive. If other organizations were refocusing themselves towards the poor, the relationships between poverty focus and changing poverty focus should be low or even negative. The latter pattern would give the strongest evidence of nonprofits taking on major new responsibilities towards the poor.

I developed two measures of changing poverty orientations: changes in target focus and expansions in programs of most direct concern to the poor (basic needs and employment).[22] Both of these change measures show moderately positive relationships to poverty focus (see last two columns of Table 2) suggesting that most of the changes occurred among those nonprofits which were already predisposed towards the poor and their problems.

As shown in Table 3, about one-quarter of the organizations reported (in 1984) that they had increased their target focus at least somewhat on some vulnerable target groups: poor, blacks, unemployed, or single-parent families, although only a small proportion reported much more focus on these groups. TARGCHG summarizes the target shifts for these four groups and ranges from 1 (much less emphasis on all four groups) to 5 (much more emphasis on all four groups),[23] with a mean of 3.3 and median of 3 (no change). Only 18 percent of the organizations scored 3.5 or above, indicating that relatively few organizations reported substantial increased targeting on these vulnerable groups. Similarly, only 28 percent of the organizations reported at least one program expansion or program start that involved providing for basic needs or helping people with employment problems, two areas of high priority concern for the poor.[24]

<<Table 3 About Here>>

These findings suggest that, however measured, nonprofits were not primarily concerned with low income populations and their problems, even during this period of high levels of poverty and extensive hardship. Nor did a large proportion of them shift their efforts significantly in the direction of providing more services to the poor, although they were called upon by both public and private leaders to do so. Moreover, those that appeared to have made the largest efforts to increase their focus on the poor were also the ones that were already concerned with these issues.

EXPLAINING THE POVERTY FOCUS OF NONPROFIT ORGANIZATIONS

To examine the reasons for these patterns in greater detail, I explored different hypotheses about sources of influences on organizational orientations. I focus on the fit between organizational characteristics and poverty focus and assume that poverty orientations reflect a selective process of decision-making and actions. Appendix Tables A and B presents the zero-order correlations between the dependent variables and the independent variables discussed below.

The Poverty Focus of Nonprofits Reflect Community Needs. As mediating institutions nonprofits respond to community needs, including the needs of the poor. Therefore, the greater the community needs, the more likely the organization is to have a poverty focus and to move further in that direction. I have no direct measure of community need,[25] but rely on the organization's 1982 and 1984 report on service demands during the previous year. SERVDMND measures persistent changes in demands for those two years, ranging between 1 for persistently decreasing service demands and 5 for persistently increasing service demands.[26] I expect SERVDMND to be positively related to poverty focus and to increased poverty focus.

Community needs should be experienced more forcefully by those nonprofits that maintain close contacts with the local community, with particularly vulnerable population groups, or participate most actively in public policy advocacy.[27] Thus, poverty focus should relate positively to the percent minority on the board (BOARD_MIN), a director active in community or church work (DA_COMMWK), or in politics (DA_CONECT), agency participation in public policy protests or actions (POLACTSC), use of formal needs assessments (NEED_ASMT) or systematic client surveys (NEED_CLI) to determine client needs, and adding or plans to add clients or community representatives to the board (BOARD_CLI). These variables should also relate positively to increased poverty focus.

Those organizations that actively use outreach and evaluation efforts should experience the community pressure more directly and change their poverty focus accordingly. Consequently, nonprofits that expanded their program/need evaluation efforts (EVAL_EFF), make themselves accessible to clients through outreach efforts such as referral systems (OUT_REF), advertisements (OUT_ADS), or contacts with the community (OUT_LINK), should have increased their poverty focus the most.

Nonprofits are Captured by the Circumstances of Their Historical Past. The population ecology theory argues that organizations are born in response to environmental circumstances to fill environmental niches, and find it difficult to change their core aspects (purpose, technology) because early practices become precedents for subsequent decisions.[28] Thus 80 percent of nonprofits establish their primary target group when founded or reorganized. If organizations are captured by their past in this manner, then those that were established during periods of major concern with the poor should still exhibit the strongest commitment to them. POVCOHRT measures whether the organization was established during the 1930s or the 1960s, periods when poverty was of intense public concern, and should be positively related to poverty focus and negatively related to increased poverty focus.

As Resource Dependent Organizations the Actions of Nonprofits Reflect the Types of Resources to Which They Have Access.[29] Because poor people have limited resources to pay for services, nonprofits with access to "subsidies" to help finance their operations should be better able to focus on the poor. Similarly, an increase in "subsidy" income should allow for more attention to the poor. Therefore, organizations that rely most on donations or government contracts (GOVDON%) and least on fee income (FEE%), whose directors maintain intense contact with foundations or corporate givers (EX_FNDR) or previously worked for such funders (DA_FNDREL), or which added or plan to add board members with government, foundation, or corporate contacts (BOARD_GFN) will have the greatest poverty focus. Those with the greatest linear increases[30] in subsidy income (GOVST_SL, DONST_SL) should be best able to increase their poverty focus and those with high fee increases (FEEST_SL) least able to do so.

Contacts with "subsidy" funders develop over time and are more accessible to larger organizations. Larger organizations may also have more diverse resources and be more flexible in using them, while those that operate with some degree of formalization may use resources more efficiently.[31] Therefore older (ORG_AGE), larger (LNSIZE)[32] and more formalized (ORG_PROC) organizations will be more poverty oriented and better able to increase their poverty attention.

Nonprofits that Most Strongly Endorse Professional Management and Service Models Will be Less Concerned with the Poor. Low income groups are difficult to serve. Their problems may not lend themselves effectively to the professional counseling model, they may not have the vocabulary and presence to work effectively with specialists, and they may impart their stigma to the agency and its personnel.[33] The difficulty of working with the multitude of problems the poor have and the crisis nature of many of those problems, complicate management and record keeping procedures. At the same time nonprofits are under increasing pressure to improve their management standards,[34] sometimes as a condition of obtaining funding. This suggests that organizational and professional procedures may not only serve as the means by which nonprofits work to achieve their official goals, but may become goals in their own right, replacing the original purpose of the organization in shaping organizational decision-making.[35] Therefore, nonprofits that are most professionalized (PROF_STFF), staff run (STFF_RUN), concerned about adding board members with business or professional expertise (BOARD_EXP), or insistent about maintaining organizational records (ORG_RCRD) should be least poverty oriented and least likely to increase their poverty orientation.

The Extent to Which Nonprofits Are Oriented Towards Other Nonprofits May Detract from Their Focus on the Poor. Organizations compete not only for external resources, such as funding and clients, but for power and prestige. In an institutionalized nonprofit sector, such as that of Chicago,[36] nonprofits form federations and coalitions,[37] not only to pursue external policy issues on behalf of their clients or help solve internal management problems, but because such efforts increase their visibility among their peers and provides them the opportunity to demonstrate leadership and influence. Such interorganizational contacts also serve as important assets in the competition for scarce resources.[38]

Federations and coalitions aim to mobilize their participants, develop comprehensive agendas and facilitate effective action. However, the agendas may not focus on the poor, and the interorganizational relations may become goals in their own right because of the benefits they bring to participants. If true, the more directors interact with directors and staff in other nonprofits or public agencies (EX_GVNP), the more active the organization is in nonprofit affiliations or lobbying efforts (ORG_AFF), the more extensive its contacts are with other nonprofits in sharing resources, board members, programs, etc (ORGNETSC), the broader its board mix (BOARD_MIX) and the more it looks to other nonprofits to determine client needs (NEED_LEG), the less poverty oriented the organization will be. The relationship between such nonprofit institutional relations and changes in poverty focus is less clear. Such efforts may marginally increase an organization's ability to devote more resources to the poor and disproportionately attract nonprofits able or willing to change their orientations.

FINDINGS

The zero-order correlations between the independent variables outlined above and the two sets of dependent variables, extent of poverty focus and of increase in poverty focus, show that although only some of the relationships are confirmed, almost all of these are as predicted. Six of the 27 relationships between POVTARG and the independent variables are significant and all are as predicted (see Table A in the Appendix). The same pattern holds for seven correlations for POVNEED and for six correlations for POVSTRAT. Measures of community need and resource dependency dominate in all three cases. The results for the two measures of poverty client contacts are somewhat more problematic, especially the 1982 measure. POOR82 is significantly correlated with ten independent variables, but only six of these are as predicted. POOR85 is significantly related to seven independent variables, but one of these is opposite of what was predicted.[39] Given the likely measurement problems in these two dependent variables, these uneven findings are perhaps not unexpected.

The patterns for increased poverty focus are also mixed with relatively few significant correlations. TARGCHG is significantly related to nine of the 34 independent variables, seven of which are from the community needs and resource relations hypotheses and as predicted, while the two variables from the professional/management and nonprofit network hypotheses are contrary to expectations. Efforts to expand or start poverty related programs show similar patterns. #POVPRG is significantly related to seven of the independent variables from the community needs and resource relations models, all as expected, and to five variables from the professional/management and nonprofit network hypotheses, but only one of these, PROF_STFF, as expected. These findings give credence to the importance of community needs and resource dependency in moving nonprofits towards greater concern with the poor and their problems. Management and professional commitments and involvement in nonprofit networks do not appear to impede such changes.

Predicting Poverty Focus: Findings and Discussion

To look at the joint operation of the independent variables I undertook a series of stepwise regression analyses.[40] Table 4 shows the result for the five dependent variables measuring poverty focus. The amount of variance explained ranges between 24 and 42 percent, the results generally confirm the patterns from the zero-order analysis, and with one exception all the standardized regression coefficients are consistent with the hypotheses outlined above.

<<Table 4 About Here>>

Resource and community relations appear to be important factors. Some measure of resource dependency appears in every equation. This points to the importance of "subsidies," and of close relationships with those who provide them, in maintaining poverty orientation. In addition, large organizations appear consistently more poverty oriented than smaller ones,[41] presumably because they have a greater variety of resources available and must be particularly sensitive to issues of legitimacy in maintaining donor support. Nonprofits also appear to function as adaptive mechanisms to community needs, although the process is mediated through contacts with vulnerable groups and other community institutions. This suggests that organizational decision making about maintaining and developing such links plays a key role. Direct service demands do not enter into any of the equations.

Nonprofit imbeddedness in the sector's institutional relations may limit poverty focus, perhaps because of goal displacement, or because of a nonprofit institutional "culture" which does not incorporate a strong commitment to the poor or their problems. Whatever the explanation, the findings have important policy implications. They suggest that the nonprofit sector mirrors government and the private sector in devoting most of its resources and concern to middle and upper income groups. The Reagan appeal to nonprofits to take greater responsibility for the poor creates not only practical problems in terms of resources to do so, but institutional problems as well.

Only one measure of management or professional commitments, adding or seeking board members with professional or business expertise (BOARD_EXP), entered an equation, namely that for POVTARG. However, the relationship was positive, not negative as hypothesized. Perhaps that is because nonprofits with the strongest poverty focus experienced the highest persistent loss of total revenues over the 1981-84 period[42] and encountered the greatest turbulence in their major sources of funding, especially government.[43] These organizations faced obvious resource problems and might well seek board members with management expertise to deal with them.

Predicting Changing Poverty Focus: Findings and Discussion

Table 5 presents the stepwise regression results for the two changes in poverty orientation variables. Respectively two and three variables enter the final prediction equations, explaining 23 and 17 percent of the variance. All but one of the standardized regression coefficients are all as hypothesized. The ambiguities of the zero-order correlations between poverty changes and measures of management and professional commitments and nonprofit networks surface only to a limited extent.

<<Table 5 about here>>

The extent of change in target focus on vulnerable groups (TARGCHG) is positively related to the extent of persistent service demands on the organization and to increased government funding. These findings confirm that nonprofits are responsive to community needs and serve as adaptive mechanisms, but they depend on government funding to extend their efforts towards the poor. The sector has been unable or unwilling to articulate a call on its other funding sources to facilitate such efforts.

Organizations that moved to add board members from the world of foundations, corporate giving, or government grants developed programs in basic needs or employment (#POVPRG), as did those that devoted increased resources to program evaluations, in the latter case perhaps because they encountered the need for them. Major cuts in government spending for employment and training, shifts in public policies to directly involve the business sector in job programs, and growth in public funding for food and shelter, gave greater salience to nonprofit contacts with key funders if they were to develop programs of this type. Finally, nonprofits with the most professional staff were least likely to develop programs of direct concern to the poor, probably because basic needs programs and the new emphasis on OTJ training require relatively few professional services.[44]

CONCLUSIONS

The Reagan policy changes of the early 1980s presented a natural experiment on how nonprofits operate. Poverty and serious needs were increasing at the same time as their government support declined. Caught between these two countervailing demands, nonprofits had several options open to them: convince private donors to provide greater support for their work with the poor, activate nonprofit networks to find solutions to the problems of poverty and declining public spending, and institute management or professional strategies to use resources more effectively in meeting the problems of the poor.

As my findings show, these options were unrealistic since only a minority of nonprofits focus on the poor and their problems and relatively few made significant efforts to move in that direction during the early to mid-1980s. To explain these patterns I drew upon five models of nonprofit organizations: as adaptive institutions to community needs, as captured by their historical origins, as resource dependent organizations, as committed to professional and managerial models, and as imbedded in nonprofit institutional relations.

My findings lend at least partial support to all but the second model, especially the resource dependency model. Access to subsidy revenue in the form of government funding or private donations clearly shapes the poverty focus of nonprofits. The goal displacement theories, that professional or management models or imbeddedness in nonprofit networks take precedence over commitment to the poor, receive more mixed support. These forms of organizational commitments appear most extensive among those with the least commitment to the poor and their problems, but appear to facilitate the movement of nonprofits towards greater poverty focus. Nonprofits also respond to community needs, but mainly as these are expressed through the specific relationships nonprofits maintain with community representatives or institutions. Nonprofits are not as responsive to the poor as public stereotypes might suggest, probably because they have enough to do without focusing on the poor and their difficult problems. Nonprofits see their own problems as lack of resources, not misdirected efforts. Indeed, a large proportion (80 percent) of directors said the organization was limited in its ability to serve its major target group by the resources available to it.

In economic terms, nonprofits are faced with excess market (service) demands, reflecting both low levels of public spending for human services and elastic demands. As a result they have no market test for their effectiveness.[45] They can almost always point to meeting some "important" need and often report more clients than expected when they start or expand programs (36 percent). These features encourage nonprofits to limit their outreach (most rely on word of mouth or inclusion in formal directories) and help explain why relatively few of the poor have access to and make use of nonprofit service providers.[46]

The policy implications of these findings are obvious. The Reagan hope that nonprofits could take a more active role in caring for the poor and maintain the social safety net ignored the extent to which nonprofits depend on government funds to operate. The policy also falsely assumed that nonprofits have a strong commitment to the poor that is independent of the incentives provided by government funding and that they would be able to move further in that direction. Perhaps nonprofits were the victims of public perceptions that they serve the poor. The Reagan administration took them seriously.

NOTES

[1] Nonprofit organizations that provide human services, excluding membership associations, social clubs, churches, hospitals, arts, cultural, education and research organizations. See Gronbjerg, 1986.

[2] In 1981 and 1982 75 percent of articles about nonprofit human service providers in the Chicago Tribune and the Chicago Sun-Times included the theme of service to low income or "inner city" residents.

[3] Jencks, 1987, reports that the presence of low income populations appears to increase individual giving in a community.

[4] Rather, nonprofit leaders react strongly to any suggestions that the sector does not actively serve the poor. See, Skelly 1986.

[5] Neither is dependent on the profit incentive nor subject to the disciplines of the free market (see Douglas, 1983) and both aim to achieve substantive goals (see Rushing, 1976, Kahlberg, 1980).

[6] See Rose-Ackerman, 1986, Hansmann, 1980, 1987, Weisbrod, 1974, 1977, and Douglas, 1987, for a discussion of these issues.

[7] I.e., universities, private schools, hospitals, and organizations providing primarily arts, culture, education and research services.

[8] I.e, Hawley, 1950. In practice, human ecology has paid little attention to nonprofits and their adaptive response. Most community studies, e.g., Fuguit and Kasarda, 1981, Yancey and Ericksen, 1979, focus on business and government or look at voluntary membership associations as mediating between the community and public policy formulation. See Taub et al., 1977. None of these efforts address the extent to which nonprofit human service organizations constitute specialized adaptive mechanisms that supplement, compete with, or operate on par with governmental agencies and private businesses.

[9] The organization literature has only recently focused on nonprofits as a specialized institutions, but rarely distinguishes between them and public agencies. Both are seen as nonprofits that endorse goals and principles of decision-making that differ in fundamental ways from those of for-profits, although many nonprofits have profit-making activities as Salamon et al., 1986 show. Major developments in the field, i.e., concern with resource dependency, (see Pfeffer and Salancik, 1978), organizational environments (see Hannan and Freeman, 1977, 1984, Aldrich, 1979), and institutional models of organizational behavior (see Meyer and Scott, 1983, DiMaggio and Powell, 1983) have either emerged out of studies of nonprofits or drawn attention to differences between them and businesses.

[10] See Pfeffer and Salancik, 1978, DiMaggio and Powell, 1983.

[11] I do not directly measure extent of community needs in this study, but argue that Chicago nonprofit human service organizations have had both the occasion and time to develop a focus on the poor and their problems. My approach is to examine the extent to which they have done so and the organizational factors that appear to shape their poverty orientations.

[12] Somewhat less of the public spending goes to nonprofits outside of health services. See Gronbjerg et al., 1984.

[13] See Gronbjerg et al., 1985.

[14] See Hemmens et al., 1986, Stagner and Richman, 1986, Cook et al., 1986.

[15] See Gronbjerg, 1987, and Salamon et al., 1987, for specifics.

[16] The 149 agencies located in Cook County, whose major service activity was not arts, culture, recreation, education, research, or long term health care, and which had responded to the two prior waves of mail questionnaires. See Gronbjerg et al., 1985, Gronbjerg, 1986.

[17] The universe is described in Gronbjerg et al., 1985, and Gronbjerg, forth.

[18] For a discussion of "core" and "peripheral" types of organizational characteristics, see Hannan and Freeman, 1984, and Singh et al., 1987.

[19] This is the primary measure of poverty orientation used by The Urban Institute in its analyses. See Gronbjerg et al., 1985.

[20] Our attempt to check potential inconsistencies by going back to the organizations revealed major uncertainties on their part about the "actual" data. We could confirm only a small minority of the inconsistencies as actual changes.

[21] Cynics might argue that such poor data reflect the need for nonprofit to obscure their lack of direct involvement with the poor in order to safeguard their own legitimacy among donors.

[22] The problems in the client data appeared so serious that I did not use any direct measures of changes in client composition.

[23] Those responding "not applicable" were coded as 3, or "no change," to minimize potential bias.

[24] See Hemmens et al., 1986, Stagner and Richman, 1986.

[25] The characteristics of the community in which the organization is located may not be an adequate measure of community pressure. Only one-quarter of nonprofits define themselves as serving a local community, the rest identify a larger geographic region as their service area. Also, 26 percent of the interviewed organizations, including several with a major focus on the poor, are headquartered in the Loop or Near North Side.

[26] Only 6 percent of the organizations scored less than 3 (declining demand), while 26 percent scored 5.

[27] See Corwin, 1972, Meyer, 1982, Hasenfeld, 1972.

[28] See Hannan and Freeman, 1977, 1984, Singh et al., 1987, Kimberly, 1975, Kaufman, 1984, Carroll and Delacroix, 1982.

[29] Pfeffer and Salancik, 1978, Dess and Beard, 1984.

[30] Nonprofits operate in extremely turbulent resource environments with considerable year to year fluctuations. To separate turbulence from linear changes, I regressed inflation adjusted total revenues (and each source of founding) on year (1981-84). I then used the ratio between the standardized regression coefficient and average revenues as a measure of resource change and the unexplained variance from the regression analysis as a measure of funding turbulence.

[31] Baldridge and Burnham, 1975, Rowan, 1982.

[32] The natural log of inflation adjusted average income (1981-84) avoids the confounding effects of funding fluctuations and a skewed income distribution.

[33] Cloward and Epstein, 1965.

[34] Hall, 1987.

[35] Hall, 1987, Scott, 1967, Dess and Beard, 1984, DiMaggio and Powell, 1983.

[36] The sector counts about 3,000 service organizations in the metropolitan area, an additional 1,000 schools, universities and hospitals, 5,500 churches, an unknown number of social clubs, fraternal organizations, and membership associations, about 1,200 foundations and trusts, and 100 United Way organizations.

[37] The 128 interviewed organizations were members of 112 separate federations or coalitions, not counting United Ways and major religious federations.

[38] Pfeffer and Salancik, 1978, Caroll, 1981, Dess and Beard, 1984, Provan et al., 1980, Pfeffer and Leong, 1977.

[39] Organizations that serve middle or upper income clients may be especially likely to incorporate client representatives on their boards, not only to serve as effective spokespersons for the organization, but to solidify client loyalties.

[40] I used fairly stringent criteria for inclusion (significance level of .05 or better) and exclusion (.055) of the independent variables.

[41] This is the case even when single-purpose day care centers, some of the smallest and most fee oriented organizations, are excluded from the analysis.

[42] Zero-order correlations between the five dependent variables and the standardized regression slope for revenues (adjusted for inflation) on year ranged between $r = -.22$ ($p<.05$) and $r = -.32$ ($p<.01$).

[43] Zero-order correlations between turbulence in government funding and poverty focus ranged between .20 and .25 ($p<.05$) for POVTARG, POVNEED, POVSTRAT, and POOR85. The correlation for POOR82 was .13 (not significant). Turbulence in donation funding correlated significantly and positively only to POVSTRAT ($r = .23$, $p<.05$). Turbulence in fee income correlated significantly and negatively to all measures of poverty focus and ranged between -.22 and -.40. The stability in fee income reflects low reliance on fee income by these organizations.

[44] Orfield et al. (1986) argue that the Job Partnership Training Act programs are much more likely to "cream" the clients, i.e., serve those least likely to need extensive supplementary services, than were their predecessor CETA programs.

[45] Kanter, 1979.

[46] Cook et al., 1986, Hemmens et al., 1986, Stagner and Richman, 1986.

TABLE 1

EXTENT OF POVERTY FOCUS AMONG CHICAGO NONPROFITS

Poverty Focus Measure (n)	Percent of Organizations
Poverty Composition of Primary target Group (119) (POVTARG)	
Entirely Low-Income	23%
Partially Low-Income	44
Not Low-Income	34
Perceived Poverty/Service Need Relationship (120) (POVNEED)	
Direct Link	18%
Some Relationship	35
No Relationship	48
Poverty Directed Service Strategy Endorsed (120) (POVSTRAT)	
Basic Needs and Employment Help	17%
Other Poverty Intervention	38
No Poverty Intervention	46
Proportion of Clients Poor, 1982 (102) (POOR82)	
75% or more	23%
50-74%	14
25-49%	13
10-24%	16
Less than 10%	34
Proportion of Clients Poor, 1985 (91) (POOR84)	
75% or more	36%
50-74%	12
25-49%	13
10-24%	12
Less than 10%	28

SOURCE: Urban Institute Nonprofit Sector Project

TABLE 2

ZERO-ORDER CORRELATIONS OF MEASURES OF POVERTY FOCUS

Variables	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Extent of Poverty Focus							
(1) POVTARG	1.00	.75**	.62**	.64**	.80**	.39**	.28**
(2) POVNEED		1.00	.78**	.58**	.70**	.30**	.36**
(3) POVSTRAT			1.00	.43**	.58**	.26**	.43**
(4) POOR82			1.00	.85**	.21*	.29**	
(5) POOR85				1.00	.27**	.30**	
Change in Poverty Focus							
(6) TARGCHG						1.00	.26**
(7) #POVPRG							1.00

NOTE: correlations based on Ns that range between 90 and 120.
* Significantly different from zero at p<.05
** Significantly different from zero at p<.01

SOURCE: Urban Institute Nonprofit Sector Project

TABLE 3

CHANGES IN POVERTY FOCUS AMONG CHICAGO NONPROFITS

Change in Poverty Focus Measure (n)	Percent of Organizations
Change in Target Focus on Blacks (122)	
Much More emphasis	7%
Slightly More Emphasis	20
No Change	67
Slightly Less Emphasis	1
Much Less Emphasis	0
Not Applicable*	14
Change in Focus on Low-Income (120)	
Much More Emphasis	12%
Slightly More Emphasis	10
No Change	54
Slightly Less Emphasis	4
Much Less Emphasis	0
Not Applicable*	19
Change in Focus on Single-Parent Families (120)	
Much More Emphasis	8%
Slightly More Emphasis	17
No Chang	53
Slightly Less Emphasis	0
Much Less Emphasis	0
Not Applicable*	22
Change in Focus on Unemployed (120)	
Much More Emphasis	8%
Slightly More Emphasis	12
No Chang	52
Slightly Less Emphasis	2
Much Less Emphasis	0
Not Applicable*	25
New or Expanded Programs (#POVPRG) (128)	
3+ New/Expanded Basic Needs or Employment Programs	6%
2 New/Expanded Basic Needs or Employment Programs	9
1 New/Expanded Basic Needs or Employment Programs	13
No New/Expanded Basic Needs or Employment Program	72

* Recoded as "no change."
SOURCE: Urban Institute Nonprofit Sector Project

TABLE 4

STANDARDIZED REGRESSION COEFFICIENTS IN FINAL PREDICTION EQUATIONS FOR POVERTY FOCUS

	Dependent Variables				
In Equation	POVTARG	POVNEED	POVSTRAT	POOR82	POOR85
Community Pressure					
+ BOARDMIN		.24*	.23*		.26**
+ POLACTSC	.34**				
+ DA_COMMWK		.26*			
+ NEED_CLI					.21*
Resource Relations					
+ GOVDON%	.44**		.26*		
- FEE%	-.37**		-.30**	-.34**	
+ EX_FNDR			.27**		
+ LNSIZE	.39**	.23*		.42**	.24*
Management/Professional					
- BOARD_EXP	.27**				
Nonprofit Network					
- ORG_AFF	-.22*				
- ORGNETSC	-.26*				
- NEED_LEG			-.21*		
Multiple R .68**	.54**	.53**	.54**	.62**	
R Squared (adj)	.42	.25	.24	.27	.36

NOTE: The sign next to each independent variable specifies the hypothesized relationship. N = 76. * p < .05; ** p < .01.

SOURCE: Urban Institute Nonprofit Sector Project

TABLE 5

STANDARDIZED REGRESSION COEFFICIENTS IN FINAL PREDICTION EQUATIONS FOR INCREASED POVERTY FOCUS

	Dependent Variables	
Variables In Equation	TARGCHG	#POVPRG
Community Pressure		
+ SERVDMND	.44**	
Outreach Efforts		
+ EVAL_EFF		.27*
Resource Relations		
+ GOVST_SL	.24*	
+ BOARD_GFN		.22*
Management/Professional		
- PROF_STFF		-.29**
Multiple R	.50**	.45**
R Squared (adj)	.23	.17

NOTE: The sign next to each independent variable specifies the hypothesized relationship. N = 76. * p < .05 ** p < .01

SOURCE: Urban Institute Nonprofit Sector Project

APPENDIX TABLE A

ZERO-ORDER CORRELATION COEFFICIENTS BETWEEN POVERTY FOCUS AND INDEPENDENT VARIABLES

	Dependent Variables				
Variables	POVTARG	POVNEED	POVSTRAT	POOR82	POOR85
Community Pressure					
+ SERVDMND	.18	.24*	.18	.09	.14
+ BOARD_CLI	-.16	-.14	-.09	-.30**	-.26*
+ BOARDMIN	.30**	.32**	.29**	.23*	.36**
+ DA_COMMWK	-.10	.11	.03	-.23*	-.18
+ DA_CONECT	.09	.16	.21*	.16	.17
+ POLACTSC	.24*	.16	.21*	.14	.12
+ NEED_ASMT	-.01	-.00	.03	.15	.12
+ NEED_CLI	.18	.11	.14	.21*	.35**
Past Environment					
+ POVCOHRT	.13	.08	-.03	.07	.04
Resource Relations					
+ GOVDON%	.46**	.34**	.36*	.30**	.42**
- FEE%	-.44**	-.36**	-.35**	-.33**	-.45**
+ EX_FNDR	.28**	.20*	.30**	.18	.15
+ BOARD_GFN	-.02	.06	.10	.13	.01
+ DA_FNDREL	-.01	-.12	-.04	.06	.07
+ ORG_AGE	.01	.06	-.12	.28**	.22*
+ LNSIZE	.30**	.21*	.14	.44**	.31**
+ ORG_PROC	.14	.12	.19	.17	.20*
Management/Professional					
- ORG_RCRD	-.05	.05	.10	.12	.03
- PROF_STFF	-.09	-.22*	-.04	-.07	-.06
- STAFF_RUN	.12	-.01	-.14	.28**	.06
- BOARD_EXP	.10	.10	.08	.10	.10
Nonprofit Network					
- **EX_GVNP**	.12	.02	.02	.24*	.09
- **ORG_AFF**	.01	.01	.01	.13	.18
- **ORGNETSC**	-.14	-.13	-.08	.00	-.08
- **BOARD_MX**	-.00	-.08	-.02	.10	-.05
- NEED_LEG	.04	-.08	-.17	.13	.03

NOTE: The sign next to each independent variable specifies the hypothesized relationship. N = 76. * p < .05 ** p < .01

SOURCE: Urban Institute Nonprofit Sector Project.

APPENDIX TABLE B

ZERO-ORDER CORRELATION COEFFICIENTS BETWEEN INDEPENDENT VARIABLES AND INCREASED POVERTY FOCUS

	Dependent Variables	
Variables	TARGCHG	#POVPRG
Community Pressure		
+ SERVDMND	.44**	.26**
+ BOARD_CLI	-.05	.01
+ BOARDMIN	-.05	.01
+ DA_COMMWK	.21*	.07
+ DA_CONECT	.18	.40**
+ POLACTSC	.14	.15
+ NEED_ASMT	.22*	.36**
+ NEED_CLI	.11	.30**
Outreach		
+ EVAL_EFF	.12	.35**
+ OUT_REF	.11	.06
+ OUT_ADS	.14	.14
+ OUT_LINK	.28**	.14
Past Environment		
- POVCOHRT	-.18	-.13
Resource Relations		
+ GOVDON%	.12	-.06
- FEE%	-.14	-.01
+ TOTST_SL	.04	.01
+ GOVST_SL	.23*	.07
+ DONST_SL	.10	.11
- FEEST_SL	-.14	-.14
+ EX_FNDR	.18	.17
+ BOARD_GFN	.14	.14
+ DA_FNDREL	-.02	-.12
+ ORG_AGE	.04	.09
+ LNSIZE	.14	.19*
+ ORG_PROC	.19*	.23*
Management/Professional		
- ORG_RCRD	.19*	.21*
- PROF_STFF	.17	-.24*
- STAFF_RUN	-.06	-.05
- BOARD_EXP	.08	.21*

APPENDIX TABLE B -- Continued

ZERO-ORDER CORRELATION COEFFICIENTS BETWEEN INDEPENDENT VARIABLES AND INCREASED POVERTY FOCUS

	Dependent Variables	
Variables	TARGCHG	#POVPRG
Nonprofit Network		
- EX_GVNP	.14	.20*
- ORG_AFF	.04	.23*
- ORGNETSC	.21*	.14
- BOARD_MX	.17	.09
- NEED_LEG	.16	.08

NOTE: The sign next to each independent variable specifies the hypothesized relationship. N = 76. * $p < .05$ ** $p < .01$

SOURCE: Urban Institute Nonprofit Sector Project

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PHILANTHROPIC PRIORITIES:
THE CASE OF POOR AND LOW-INCOME CLIENTELE

by

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Philanthropic giving is often labeled as "charity". Charity to most people conjures up images of the affluent helping the poor. (Jencks, 1986, p. 322) Data on the distribution of philanthropic resources suggests, however, that by far the largest segment of philanthropy does not directly serve, advocate for, or organize the poor. I explore this phenomenon in this paper. First, I review some of the available information on the topic: what do we know about how much of the philanthropic effort is directed toward poverty? What pressures presently exist for increasing attention to poverty? Next, I apply existing history and theory of the philanthropic sector to try to understand more about why attention to poverty has taken the form it has. Finally, I consider how the alleviation and eventual end of poverty might become a higher priority on the philanthropic agenda.

My major argument here is that the relative neglect of poverty by mainstream philanthropy can be explained in part by how scholars and practitioners have conceptualized philanthropy. I focus on two issues: first, the conceptualization of relations between philanthropy and the state and politics; and second, the conceptualization of relations between donors and recipients. A shift in philanthropic priorities toward more attention to alleviating and ending poverty in the United States would, I believe, be facilitated by a reconceptualization of these relations. It should be clear that I am not arguing here for a reassertion of a traditional notion of charity in which the affluent simply give *more* to the poor than they presently do. Nor am I hearkening Reagan's call for a philanthropy that takes over for the welfare state. I am suggesting rather that a philanthropy where issues of poverty are high on the agenda will necessarily be a very different philanthropy from the one we know.

How Much of the Current Philanthropic Effort is Directed Toward Poverty and What are the Pressures for Increased Effort?

Two striking figures stand out from my review of available data on this topic: thirty percent of philanthropic organizations serve a clientele of which the majority are poor; and less than ten percent of philanthropic giving is directed toward those with a lower access to resources than the donor. The ten percent figure is an estimate from IRS data by political economist Russell Roberts, quoted by Christopher Jencks in the recent Yale University Press handbook. (Jencks, 1986, p. 322) The thirty percent figure has been widely quoted and comes from the by now well-known research of Lester Salamon and his colleagues at the Urban Institute. It is based on a survey of 3400 nonprofit organizations, including educational and cultural groups. (Salamon, 1986, p. 111). The same study found that half of so-called "charitable" organizations serve a clientele of whom only ten percent are poor.

Other data seem to confirm these figures as being on track. My own research on voluntary social service agencies, for example, suggests that the great majority of clientele of Family Service Associations are middle class. (Ostrander, 1985). National Committee for a Responsive Philanthropy researcher Scott Piepho reported in a recent paper that "a growing body of research suggests that United Ways are oriented toward serving the mainstream of society at the expense of the disadvantaged and disenfranchised." (Piepho, 1987, p. 1) Christopher Jencks in his review of who gives what to whom in the recent Yale University handbook concludes that "very few of the contributions are charitable in [the] sense [of giving to the poor]." (Jencks, 1986, p. 322). Pablo Eisenberg wrote in a recent issue of Foundation News that, "..while there have been some slight increases in money given to the poor, minorities and other disadvantaged, these constituencies and their grassroots organizations are still getting the crumbs of the philanthropic pie." (Eisenberg, Foundation News, Jan/Feb. 1987, p. 52) A paper presented at the Independent Sector Spring Research Forum in 1987, also out of the Urban Institute Study, showed--as did my research--that during the early to mid-1980's services to poor from the nonprofit sector actually declined, in part because of decreased government support. (Musselwhite and Salamon, 1987, p. 369-370)

The relatively small portion of the total philanthropic effort directed toward alleviating and ending poverty has led several scholars to suggest that the terms philanthropy and charity ought to be more carefully delineated, with the term charity reserved only for that portion of philanthropy that is specifically aimed at the poor. (Jencks, 1986, p. 322) Author of the definitive history of American philanthropy, Robert Bremner, made a similar suggestion in his 1977 paper for the Filer Commission. (Bremner, 1977, p. 98)[1]

Council of Foundations President James Joseph recently cited as one of the key trends in philanthropy the "Increased pressure...to meet needs of the most vulnerable groups." (Joseph, 1986, p. 14) One source of pressure in this direction is a real decline in public assistance at a time when poverty increased, during the late 1970's and early '80's. Poverty researcher Michael Sosin cites a 22% decline in Aid for Families With Dependent Children during the 1970's (in dollars controlled for the rapid inflation of that decade). (Sosin, 1986, p. 19) There has been, of course, increased pressure from the Reagan government for philanthropy to assume more of the responsibility for serving the poor, taking over for a welfare state Reagan wants to severely cripple if not dismantle entirely. Several authors including myself have also cited the growing need for nonprofits to legitimate their activities, to show a public on whom they are dependent for resources--whether governmental or non-governmental--that what they are doing is worthwhile. (Douglas, 1986, p.. 49; Ostrander, in press; Sosin, 1986, p.

22)

Another major factor pressing traditional philanthropy to serve, advocate for and organize the poor for social change is the "donee movement" and the kinds of alternative philanthropic groups coming out of that movement. The leading organization in this movement, the National Committee for Responsive Philanthropy (NCRP) was organized in 1977. The NCRP concerns itself with what they characterized in the first edition of their newsletter as a "considerable imbalance in philanthropic giving with the overwhelming majority of funds going to traditional organizations...and a very small proportion to advocacy organizations" serving the interests of "minorities, women and other economically and politically powerless groups." (NCRP Newsletter, Volume 1, Number 1, February 28, 1978, p. 1) NCRP has, as one of its activities, been among the leaders of a movement to allow non-United Way alternative funds to deduct voluntary philanthropic contributions from paychecks at the workplace. The alternative funds typically focus their donations on the poor and other marginalized groups. A recent booklet called Charity at Work published by NCRP describes the growing effort to institute alternative funds as payroll deductions.

One group of successful United Way alternative funds are the Black United Funds. The National Black United Fund estimates that only three percent of United Way funds go to black-controlled groups. (Charity At Work, 1986, p. 37) There are presently eight cities with a BUF, and four million dollars was raised in 1984, mostly from pay roll deductions. The BUF initiated the fight to open the Combined Federal Campaign for government workers to non-United Way charities, and former National Black United Fund President James Joseph now heads the Council on Foundations.

In addition, to NCRP and BUF, some thirty-three alternative federated funds and a number of foundations are now organized around principles like "Change not charity." (Charity At Work, p. 42) While some of the monies from these funds go to issues not directly related to poverty such as the environment and nuclear disarmament, it is likely that a significantly higher portion of resources go to groups advocating for and with poor and low income people than is the case with more established philanthropies. A Minnesota Twin Cities study found, for example, that while 25-40% of United Way funds there benefitted the disadvantaged, the figure for the cities' alternative fund (Cooperating Fund Drive) was 77%. (NCRP Newsletter, Fall 1986, p. 4)

It appears, therefore, that there is increasing pressure from a declining welfare state, from a growing problem of poverty, from some voluntary social welfare agencies' need to legitimate their activities, and from increasingly influential donee groups for established philanthropy to turn more of its attention to poverty.

What does the general public think about this issue? Joint Center for Political Studies researcher Emmett Carson found that from two-thirds to three-fourths of his sample of both blacks and whites said that the middle class is not doing enough to help the poor. (Carson, 1987, p. 3) When asked what they thought was the single most important problem for private charities to try to solve, about one in ten (9% blacks, 11% whites) said poverty was the most important. (Carson, 1987, p. 17) A recent Rockfeller Brothers Fund study reports a comparable figure to a somewhat different question. When asked, "What would you say was the main reason you gave to (name of charity)?", twelve percent (the second highest number) of respondents said "Helps poor, need, less fortunate". (Charitable Behavior of Americans, 1986, p. 23)

Much higher numbers think that caring for the poor is primarily the job of government than think it is the top philanthropic priority. In Carson's study, twice as many blacks as whites (43%; 24%) said that government must assume primary responsibility for the poor. (Carson, 1987, p. 7) A 1982 Roper poll showed 86% of Americans taking this point of view, 50% specifying they meant the Federal government. (Public Opinion, Feb/March 1982) James Joseph quotes a 77% figure for people who think that contributions to private charity should be higher and that government has the basic responsibility to care for the needy. (Joseph, 1986, p. 11) It has been quite well established that wealthy people are less likely than other income groups to think that the government should be responsible for services to the poor. (Joseph, 1986, p. 11)

While the view that government has the major responsibility for the poor might seem to suggest that philanthropy has less responsibility, I would argue that this is not a correct interpretation of these figures given the real mutual dependence between government and the voluntary nonprofit sector in social welfare. I will elaborate on this point further in the theoretical section of this paper. Suffice it to say at this point that there seems to be some support among the general public for philanthropy and government to direct more attention to the issue of poverty.

Private Philanthropy and Poverty: A Cursory Review of History

What can a cursory review of a history well-known to scholars of American philanthropy tell us about why the current proportion of philanthropic effort directed toward poverty is relatively small? And how can it help us from repeating past mistakes?

The beginning of colonial America's response to those unable to provide for their own basic needs was based in seventeenth century English poor law. According to Robert Bremner:

> All of the English mainland colonies followed the mother country's example in assigning responsibility for financing and dispensing poor relief to local authorities... Before 1820 most communities relied on informal methods [such as] auctioning off the poor, or arranging for their care by a private contractor. (Bremner, Filer Commission Report, 1977, p. 95)

About the only non-governmental organizations involved in direct responsibility for the poor at this time were church-related charities. (Katz, 1986, p. 39)

Seeing the failure of local governmental and religious charitable efforts to help the poor, welfare reformers in the 19th century sought to establish "indoor relief" or institutionalized care in public almshouses. (Bremner, 1977, p. 96) Under this plan, government would be responsible for running institutions for the most desperate poor. Private charity would care for those seen as capable of helping themselves when provided with proper moral uplift. In a dichotomous conceptualization of public and private that continues well into the present, philanthropy and voluntarism came to be seen as superior to government relief. Charity "helped" by seeking self-sufficiency. Public aid "pauperized" making the poor dependent on others. (Bremner, 1977, p. 96; Saveth, 1980, p. 80)

The leaders of private charity formed the Charity Organization Societies (COS) in 1870. These were the precursors to modern organized philanthropy. Their leaders were mostly educated men and a few notable women of the upper classes. (Saveth, 1980, p. 82) The Charity Organization Societies did not give material or economic aid. They sought rather to "coordinate, investigate and counsel" in regard to services for the poor. (Katz, 1986, p. 75) The COS volunteers (called Friendly Visitors) visited the poor in their homes and sought to befriend them and provide moral example, developing a connection between the upper and lower classes based on an assumption of class superiority. (Katz, 1986, p. 76; Saveth, 1980, p. 79) The Charity Organization Societies and the men and women who headed them opposed government aid and were successful in eliminating it in at least twelve municipalities. (Kramer, 1986, p. 241; Watson, 1971, originally 1922)

The depressions of 1873 and 1893 proved the downfall of the private Charity Organization Societies. (Katz, 1986, p. 82; Huggins, 1971, Chapter 6) Despite their failure, they held fast to their methods, continuing to oppose both public relief and the efforts of workers to help themselves through organized labor. (Huggins, 1971, p. 154) Early in the twentieth century, one COS leader, Edward T. Devine (according to Katz) confessed failure, saying:

> Our use of relief has been most sparing and timid. I am inclined to believe that we have caused more pauperism by our own failure to provide for the necessities of life, for the education and training of children, and for the care and convalescence of the sick, than we have by excessive relief... (Katz, 1986, p. 83)

Despite the failure of the private Charity Organization Societies and local governments to cope with the effects of the late nineteenth century economic depressions, efforts to deal with poverty continued to focus almost entirely around these kinds of efforts until the next great depression in the 1930's. In 1935, the United States established its welfare state with the Social Security Act, well behind most other western industrialized democracies. The welfare state expanded throughout the 1960's and 1970's and--though the causes are disputed--poverty rates also declined. By the late 1970's, poverty was again on the rise and government welfare spending was perceived as being too high. Newly elected President Ronald Reagan promised to cut welfare spending. He also called upon private charity to take on responsibility for poverty and posed the old moral agenda. For those who knew the history outlined so briefly here, it was a particularly chilling call.

An alternative history of philanthropy lies in voluntary associations formed by black Americans, beginning with the black benevolent societies of the late eighteenth and early nineteenth centuries. The founding philosophies of the Black United Funds discussed earlier in this paper emerge out of this history. The focus here was on mutual self-help among equals and self-determination through the creation of voluntary cooperative economic enterprises. (Harris, 1979, p. 611) These enterprises were complemented by the educational and literary associations run primarily by black women. (Harris, 1979, p. 615) The understanding that many leading black Americans have that solutions to poverty lie in economics and education as well as moral values, and that those solutions need to derive both from peer self-help efforts and from public efforts of government is articulated in a recent influential publication from the Joint Center for Political Studies. The publication takes off from the view of the authors that currently "more than one third of blacks are trapped in poverty, many with only dim prospects for escape." (Black Initiative and Governmental Responsibility, 1987, p. 1) The authors articulate a set of principles that moves beyond "polarized debate [about the relative merits of public vs. private efforts] that does not clarify the issues." The authors define "the role of the black community and the role of government in addressing the problems of blacks." (Black Initiative and Governmental Responsibility, 1987, Introduction)

Out of a history of white upper class organized charity--distinct from and opposed to public aid, focused on moral solutions to poverty to the exclusion of economic ones, and defined by non-reciprocal giver/recipient relations of superiority/inferiority--emerged images of private philanthropy that persist to the present day. Though we need to know much more than we do about the history and present of black philanthropy, I would hypothesize that our current images and theories of philanthropy would be very different if had they been more attentive to this history. Black philanthropy emphasizes material economic help as well as moral standards, and it is based more on mutual cooperation and exchange among peers rather than a top/down relation of charity between class unequals. Black philanthropy also seems to have been more aware of the complementary relation between public and private help.

Images and Theories of Philanthropy: Implications for Philanthropic Efforts to Alleviate and End Poverty

I want next to argue that persistent mainstream images of philanthropy from political and economic theory are in part responsible for the way in which philanthropy has dealt with poverty. I will look briefly here at only two major aspects. First, I will consider how those views from political theory that dichotomize private philanthropic and public governmental efforts--views in which voluntary philanthropic efforts are implicitly seen as superior to publicly mandated ones--contribute to limiting philanthropic efforts toward poverty. Second, I will consider how those economic theories that focus on donor motives perpetuate a non-reciprocal and hierarchical relation between donors and recipients that is not conducive or consistent with efforts against poverty.[2] I will follow this with a discussion of how it seems to me philanthropy will need to be reconceptualized if we are to address poverty in a more effective manner.

A dichotomous view of government and the philanthropic sector often implies, whether intentionally or not, a negative view of government. It explains the existence of philanthropy and voluntary nonprofits in terms of carrying out activities that government does not do or does not do well or adequately. Lester Salamon has called this kind of theory "government failure" theory. (Salamon, 1987, p. 34) A prominent political theory sharing certain assumptions with this perspective is the classical liberal pluralist explanation for the voluntary philanthropic sector. Pluralism says that this sector exists to provide a more diverse set of services and to present a wider range of points of view than government provides. (Douglas, 1987, p. 47) The implicit, and perhaps unintended, view of voluntary philanthropic activity is as superior to government. The nonprofit sector is where people are seen as contributing and doing more and better than they are required by public mandate.

Several scholars have recently shown that the view of philanthropy and nonprofits as carrying out separate and distinct activities from government is idealized, inaccurate and incomplete, both in terms of history and the present. (Gronbjerg, 1987; Hall, 1987; Salamon, 1987) Nonetheless the images persist. As social welfare scholar Ralph Kramer summarizes this idealized view:

> Government was to provide mass programs for routinized services and to meet economic needs, while voluntary social agencies would experiment, supplement, innovate, and specialize. (Kramer, 1987, p. 242)

It is not difficult to see how this dichotomous image limits philanthropy in regard to poverty. What the poor need most fundamentally is to have basic survival needs met. Meeting the basic needs of people on a daily basis is "routine." It includes substantial attention to economic needs. This view sees both of these direct service activities as outside of the realm of philanthropy. A reconceptualization of philanthropy that focuses more of our attention on poverty would need to incorporate these activities. This dichotomous view of governmental and philanthropic activity also discourages political advocacy and organizing for social change by private philanthropic groups. Advocacy targeting government is subtly discouraged by such views because government is seen in such negative ways. Political action of any kind is discouraged because philanthropy and charity are defined in such a way as to exclude politics. Others have called attention to this false distinction between philanthropy and politics. (Douglas, 1987, p. 51; Jenkins, 1987) A Child Welfare League of America pamphlet on advocacy suggests that to do direct service without also doing advocacy is rather like rescuing the victims of a collapsed auto bridge without doing anything to repair the bridge. A philanthropy with a priority of alleviating and ending poverty would include political action.

Economists have begun to pay attention to philanthropic activity only since the 1970's. (Phelps, 1975, p. 3) Some have sought to explain the existence of a nonprofit or philanthropic sector by appealing to public goods theory. This theory argues that nonprofits exist to provide services inadequately supplied by government in what I would say is a variation of the "government failure" theory discussed above. (Hansman, 1987) Other economists have focused on donor motives. They have been particularly interested in the Kantian motive for philanthropic activity. Ireland and Johnson in one of the first volumes on the economics of philanthropy claim this motive as "necessary for philanthropic action" (Ireland and Johnson, 1970, p. 20) The Kantian motive suggests that "for an individual to commit a good act, he must derive no satisfaction from the end of the act, but do the act only because he attributed the quality of goodness to the act." (Ireland and Johnson, 1970, p. 21)

Economists are, of course, aware that much philanthropic behavior does not conform to the Kantian motive. Phelps for example, poses a continuum with altruism as "an investment, a quid with some implicit or conjectured quo" at one pole, and "the altruistic act which is an unrequited transfer: the giving provides its own gratification" at the other pole. (Phelps, 1975, p. 2) Still, Kantian altruism has been a central point of departure for economic theory even if only used to then go on to develop alternative motives for donor behavior. (Phelps, 1975, p. 7)[3]

What these theories are exclusively concerned with is the philanthropic donor. The recipient is absent from this formulation, and the social relation between donor and recipient is obscured. I believe that models of philanthropy which focus exclusively on what the donor does or does not want as a condition of giving divert attention from the recipient's needs and interests. When the focus of attention is on the giver's motives, attention is diverted further from the outcome of giving from the point of view of the recipient. What did the gift actually accomplish in terms of alleviating poverty or working toward social changes that would end poverty? Models of philanthropy that focus exclusively on the donor also perpetuate a non-reciprocal and hierarchical relationship, giving the donor more power and control over what the gift is to be or whether it is given at all and how it is to be used by the donor. The only obvious power the recipient has in this model is to accept or refuse the gift as it is offered. Even the language of "givers" and "receivers" suggests a one-way relationship in which donees have nothing with which to reciprocate, in which valued goods and services move only in one direction.

This model seems to me at odds with one which would encourage optimal philanthropic efforts to alleviate and end poverty. An effective philanthropy must, as few would dispute, be centrally concerned with meeting the needs of recipients and accomplishing the goals that are set out. A society committed to ending poverty--to creating a nation in which the basic needs of every person are met--is, it seems to me, also one in which all people are seen as having a right to control their own lives. Non-reciprocal and hierarchical relations between donors and recipients are inconsistent with this vision. A reconceptualization of philanthropy that is more consistent and conducive to alleviating and ending poverty might begin by defining philanthropy as an interactive and reciprocal social relation between donor and recipient in which the needs of recipients are matched to the interests of donors. (Ostrander and Schervish, forthcoming) The final section of this paper elaborates briefly on this and other reconceptualizations suggested here.

Reconceptualizing Philanthropy: Poverty and Philanthropic Priorities

The historical and theoretical review presented here suggests three broad reconceptualizations of philanthropy which would facilitate a greater focus on alleviating and ending poverty.

We need first a view of philanthropy and the nonprofit sector that recognizes the substantial intermingling and interpenetration with government and that portrays relations between them as cooperative and overlapping rather than oppositional and dichotomous. This would encourage philanthropic activity that contributes to meeting the day to day basic needs of those who are poor, including economic needs. The resources of the philanthropic sector are, of course, in no way adequate to this enormous task. The primary responsibility here must be that of government, of a fully developed welfare state. Nonetheless, as poverty researcher Michael Sosin has shown in his book Private Benefits (1986), nongovernmental nonprofit social welfare agencies can and do contribute to the material needs of the poor. Sosin suggests that voluntary agencies can be particularly effective in providing for emergency needs for shelter, food, and clothing, perhaps while clients are awaiting public action. (Sosin, 1986, p. 112) Some of the alternative philanthropic organizations discussed earlier in this paper provide models for how the philanthropic dollar can be directed more toward these kinds of activities.

The second reconceptualization is the need to redefine charity and philanthropy in ways that incorporate political advocacy and organizing for social change. Given the relatively limited resources that are available to philanthropy and the nonprofit sector, probably the most efficient and effective use of these resources is to press other institutions in society which have sizeable resources to increase their efforts to alleviate and end poverty. While government certainly needs to be the primary target for advocacy and other political action against poverty, the large philanthropic donor organizations such as the United Way and the major foundations, and the large voluntary social welfare agencies such as those affiliated with the Family Service Association of America and the Child Welfare League of America are also appropriate targets. The donee movement discussed here has begun this effort.

The third reconceptualization of philanthropy I am suggesting is a reconstruction of the relationship between donors and recipients, a democratization of the philanthropic process. This has received relatively little attention in the scholarly literature. Lester Salamon's "voluntary failure" theory is helpful in initially laying out the undemocratic nature of the current philanthropic process. What he calls "philanthropic paternalism...vests most of the influence over the definition of community needs in the hands of those in command of the greatest resources." As a consequence of this influence by those who can and do give at the highest levels, Salamon suggests

> The nature of the philanthropic sector comes to be shaped by the preferences not of the community as a whole, but of its wealthy members. As a consequence, some services favored by the wealthy...may be promoted while others desired by the poor are held back." (Salamon, 1987, p. 41)

Salamon's description of how the philanthropic process presently operates supports one of my major points here. Philanthropy will have great difficulty in effectively addressing issues of poverty until the poor themselves and their representatives--the recipients of philanthropic activity--are at the tables where the decisions are made about where and how to direct the efforts. How philanthropy is organized will need to change. The giving and receiving of philanthropic gifts of money and time will need to be seen as an interactive, reciprocal and non-hierarchical process of negotiation between donors and recipients. What do poor recipients and the philanthropic groups that work with and for them have to contribute--to bargain with--in a process of negotiation with donors and their representatives? How might the donor/recipient relationship be seen as more mutual, as an exchange of valued goods or services?

Conceptualizing philanthropy in this way requires asking these and other questions to which we do not at present have answers. As a beginning, I would suggest that reconstruction of the relationship between donor and recipient will require an expanded notion of the public interest and the role of philanthropy in promoting it. Some scholars of philanthropy are beginning to define the public interest and public interest philanthropy not in terms of any specific policy but as expanding the points of view that are represented. (Jenkins, 1987, p. 296) This is seen as essential to creating an effective democracy that serves the needs of all who make up the public. A reconstruction of the donor/recipient relationship will also require an image of philanthropy beyond altruism as doing for others. This notion of altruism seems inevitably to dichotomize giver and receiver and to empower the giver at the expense of the receiver. It hearkens a traditional vision of charity that has been largely rejected by contemporary philanthropy, yet an alternative has not really been developed. One alternative to a self-relinquishing altruism is a notion of insurance, a kind of enlightened self-interest that does not assume an impenetrable social barrier between the poor and more affluent socio-economic classes. One might act philanthropically to protect oneself and those one cares about from becoming poor. One might act to create a society where poverty is not a risk for anyone, including oneself. A reconstruction of the relationship between donor and recipient will also require a strong organized movement of recipient groups, a movement which has already begun.

I have suggested here that it is not enough for philanthropy to simply do more to alleviate and end poverty. I have argued rather that to be effective in our efforts, we must also change how we do philanthropy--how we think about it, how we define it, and how philanthropy itself is organized and carried out.

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1. My informal and brief queries to major donor organizations in the course of writing this paper about what portion of their efforts went to alleviate or end poverty produced a list of "no information" responses. Some were themselves puzzled and said they really did not know how to define poverty. Others said they got enough hassle about all the information they required from potential donees and they didn't feel they should ask for more. Some sent long lists of their major donees and suggested that I contact them myself to ask the question. Several offered that they thought more of their resources should and would be going to serve the poor. They indicated that they felt pressed in this direction. It did not seem to me that there was any quarrel from them with data that showed the kinds of figures cited above, only that there were questions about how to find out the facts and how much and how philanthropic effort should be directed toward poverty.

2. Clearly, I do not mean to suggest that all of political and economic theories of philanthropy carry these images.

3. While I would not want it said that I am opposed to donor altruism or any other kind of altruism, I do not believe that it is a very stable or reliable source of resources for the constant and sizeable investment that the alleviation and eventual elimination of poverty requires. While we certainly can perform an altruistic act for a social equal, philanthropic altruism is a term that also conjures up images of a "do good" charity that is offensive to many. It seems to require an affluent and privileged class of donors and a disenfranchised and poor class of recipients--an image, given the concern of this paper about the paucity of philanthropic resources directed toward the poor, that is not only offensive but clearly not accurate.

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PUBLIC NEED, PRIVATE RESPONSE: PATTERNS IN THE EIGHTIES

by

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Prepared for the 1988 Spring Research Forum
"Looking Forward to the Year 2000:
Public Policy and Philanthropy"

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The appearance of this paper among a panel directed to "Public Policy and the Poor" may lead to some misunderstanding, but that in itself may prove beneficial in the end. For it is under several misconceptions that researchers using the data discussed below often labor. One purpose of this paper, beyond a presentation of the findings, is to discuss some methodological issues involved in analyzing these data, and to elucidate further their sources.

Method

The primary sources of these data are two fold: local United Way organizations and service providers, hereafter referred to as "agencies." The former are autonomous, locally-governed organizations, whose boards of directors are volunteers from their communities. Agencies are also volunteer-governed, and provide direct service to clients, whether individuals, families, groups, or the community-at-large. When United Ways provide financial support to agencies, they request data from them concerning not only expenditure of the United Way funds, but also of other sources of income. It is this sharing of financial information that makes the current research possible.

The research presented here is secondary, that is, is collected from local United Ways who, in turn, have collected some of the information from the funded agencies. The vehicle for this secondary collection is the annual survey mailed to local United Ways affiliated with United Way of America that have raised at least $100,000 in their previous fund-raising drive (the fall "campaign"). The survey underwent a name change in the period under study, from "Allocations to Agencies and Sources of Agency Income" to "Fund Distribution." (Hence the reference on the figures below.) This survey is completed voluntarily by local United Ways and therefore, never achieves a 100% response. Nevertheless, in the years cited (1981-1986), the responding United Ways represented 81% to 87% of the projected national dollars raised in their respective years' campaigns. Since local United Way organizations are not only independent of any central "headquarters" but choose to respond to each survey, the findings may be understood as aggregate descriptions of locally autonomous funding decisions by volunteers, whose United Way organizations chose to respond to the surveys.

The survey instrument itself requests information on agencies, their budgets, and the programmatic implementation of the United Way funds. The identification of agencies, for categorization purposes, is the responsibility of the responding local United Way. During the period under study, the categories changed slightly, for reasons discussed below. Nevertheless, there is enough consistency to make year-to-year comparisons meaningful.

Background of the Analysis

The much-studied shift in governmental policy toward the funding of human services which occurred during the current decade focuses more detailed attention on the role of charitable funds. While United Ways are not the only fund-raisers for human services (and they are not only fund-raisers), their national achievement and their presence in two thousand communities make them bellwethers for studying local volunteers' sensitivity to both shifts in public (here, federal) policy and in local needs. The representativeness of the agencies themselves seems reasonable, since their support portfolio resembles that of the Urban Institute sample 2/, receiving approximately 40% of income from governmental sources; their sheer number (almost 20,000 for each year) and volume of budgets ($11 billion in 1986) may represent a valid population to be studied in their own right.

Findings

There are two levels of data available for study. One is for agencies, the other, for their programs/services. Among agencies, certain categories can be used to study trends of interest. For example, agencies providing services to women in crisis ("Women's Crisis" agencies) can be studied as a separate group in these data, since they are easily identified (rape crisis center, battered women's shelters) and reliably coded by respondents. Conversely agencies can be studied by some specific names, e.g. Salvation Army, since these agencies have national identities, and are also reliably coded.

On the other level, program/service data can be aggregated according to UWASIS II 3/ groupings. For the survey, these have been modified into more general categories 4/, while maintaining the general "goal areas" of that taxonomy. While all modified UWASIS II categories are available for analysis, as are all agencies, only some are presented here.

The trends under study are those representing broad-level shifts in either perceived need or in perceived "balance". While political debate may center around their numbers, people in need of certain basic provisions, such as food and shelter, have made their presence felt in many communities. This unfortunate phenomenon is one example of a shift in perceived need. The growing presence of women in the workforce and in positions of authority has increased sensitivity to issues of "gender equity" in many arenas, including human services. Examining the shifts in funds for women's services is an examination of a shift in perceived "balance."

For conciseness of presentation, agency data are discussed first. Figure 1 displays the results of the analysis for some agencies hypothesized to reflect shifts in perceived need or balance. (While all the agencies displayed show higher levels of support in 1986 than in one of the previous years, one agency category "heart", may reflect a different shift. Rather than experiencing a decline in governmental support, these agencies may have benefited from the increasing attention to health concerns for United Ways, a trend illustrated in Figure 3). The numbers represent percentage points of total agency dollars reported in the referenced year. The three years selected represent the beginning of the current Administration's first budget; the most current year available; and a mid-period year selected for its introduction of new agency categories of interest. The figure shows that among several agencies receiving relatively high increases in United Way allocations, many are those reflecting shifts in perceived need (short-term aid; child welfare; vocational services), as well as in perceived balance (women's crisis). In order for change to have occurred, it must have been enabled by offsetting decreases for some agencies, since the total funds available always constitute 100%. 5/ To demonstrate this change, Figure 2 shows, for the years under study, many large, prevalent agencies did demonstrate a relative drop in percentage of United Way funds allocated. (While referred to as "traditional" agencies, the label is intended to connote the prevalence of such agencies in a given United Way portfolio of agencies supported; it is not intended to connote that these agencies offer services and programs which are somehow outdated.)

The second level of data analyzed, program/service, measures United Way allocations to specific activities within agencies, regardless of which particular agencies offer them. The broad UWASIS II Goal Areas pictured in Figure 3 demonstrate some shifts, although perhaps not as dramatic as those at the agency level. "Food and shelter" along with "safety and justice" often deal with clients whose fortunes have left them needing basic services. "Family services" is a large category which not only deals with the family as a client unit, but also with individuals, including children and single parents.

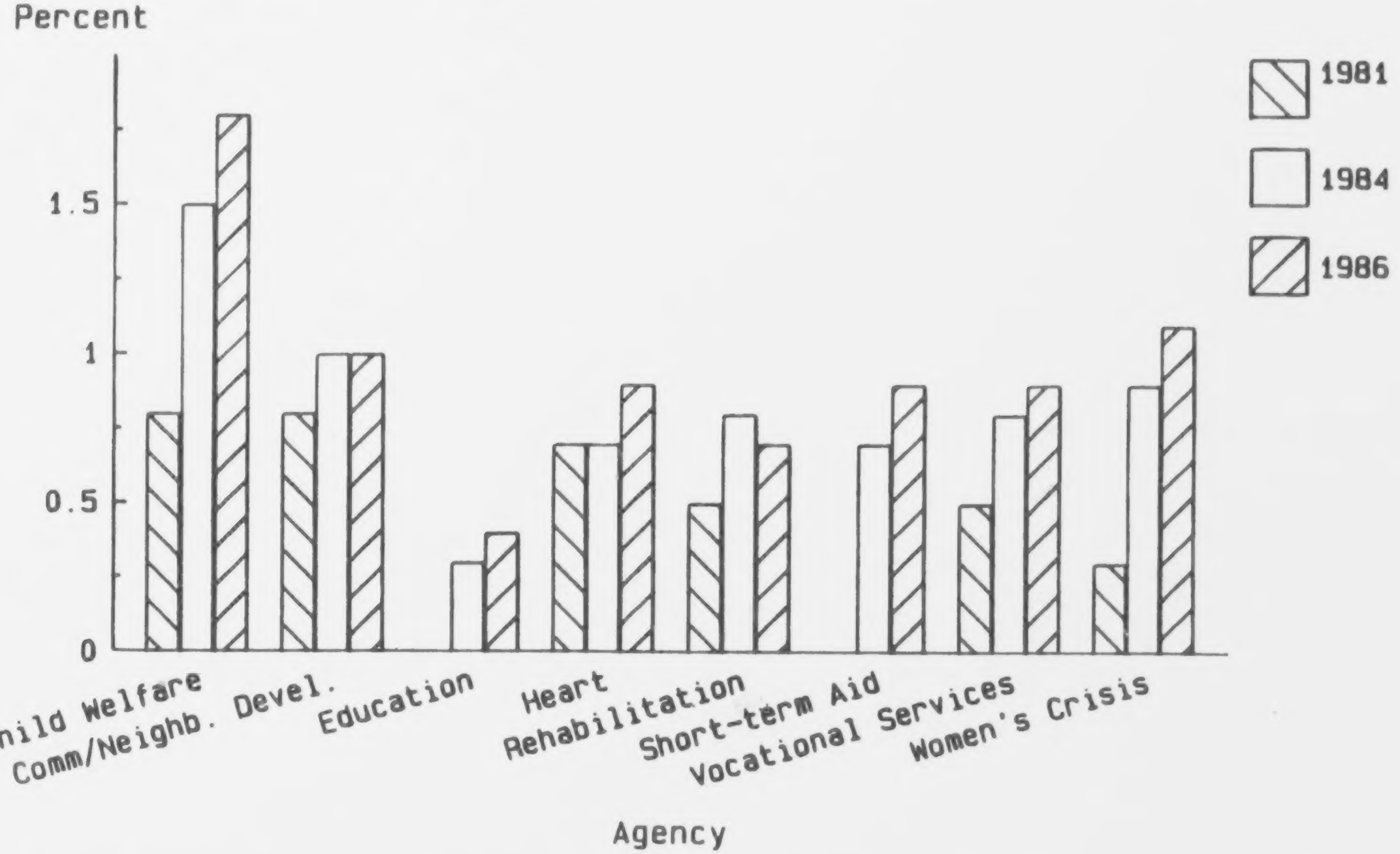
Discussion

The collective responsiveness to need demonstrated by United Ways' financial support to agencies and program/services cannot be measured in a comprehensive manner simply from aggregate figures without corresponding measures of localities' needs and the capacity of the delivery system which merits the funding, once need is determined and quantified. Nevertheless, the findings suggest that, within the limits of the methods employed, shifts in United Way allocations to agencies can be observed, and in general, appear to correspond to shifts in perceived need.

The limits of the method deserve a final discussion. As mentioned above, the survey added some agency types in 1984. This was not a haphazard decision designed to make trend analysis more difficult. Rather, new categories were needed to track new finding patterns believed to be occurring but were either submerged in larger categories, or spread across other agencies. For example, the "short-term aid" category highlights agencies whose main purpose is to provide food, shelter, and transportation. While similar agencies may have been receiving funds in the past, only for 1984 and subsequently can these specific funds be tracked. Decisions to introduce such taxonomic shifts stem from the desirability to track a relatively new, specific phenomenon, yet cloud the trend-line somewhat. However, the value of specific information appears greater than the loss of a trend-line on more global categories, especially when they may be such categories as "miscellaneous". 6/ As with funding itself, an ongoing research program needs to be responsive to ever-changing social-service phenomena.

Figure 1

Funds as a Percent of Total Annual Reported Allocations for Metros 1-8: 1981, '84, and '86
High-Growth Agencies



Education and short-term aid agencies were first tracked for the 1984 campaign.
Number of reporters 1981, 426; 1984-86, 415.

Sources: United Way of America
Profile of 1983 Allocations, Table 1
Fund Distribution Results, 1986, Table 1

Funds as a Percent of Total Annual Reported Allocations for Metros 1-8: 1981, '84, and '86 "Traditional" Agencies

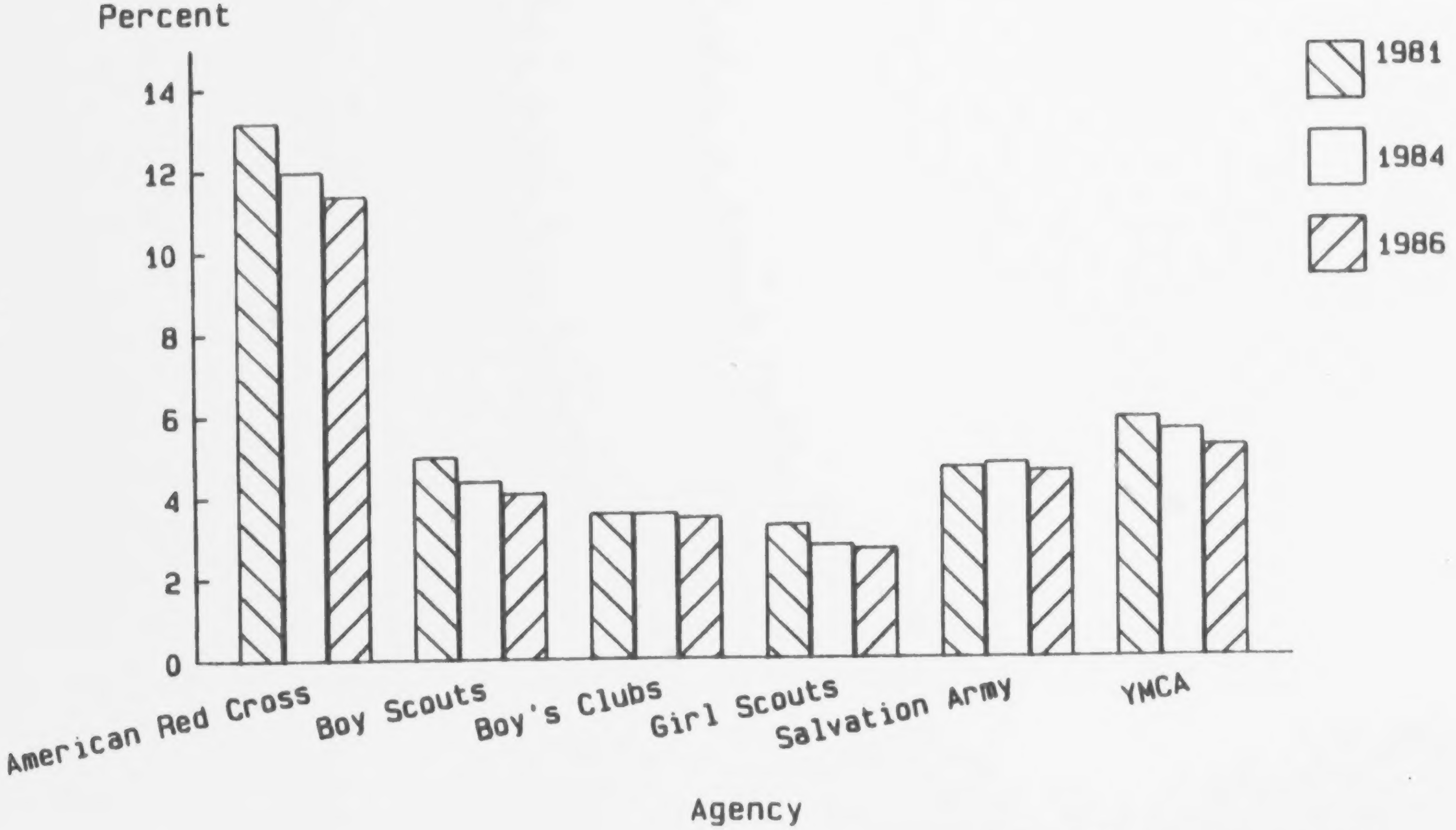


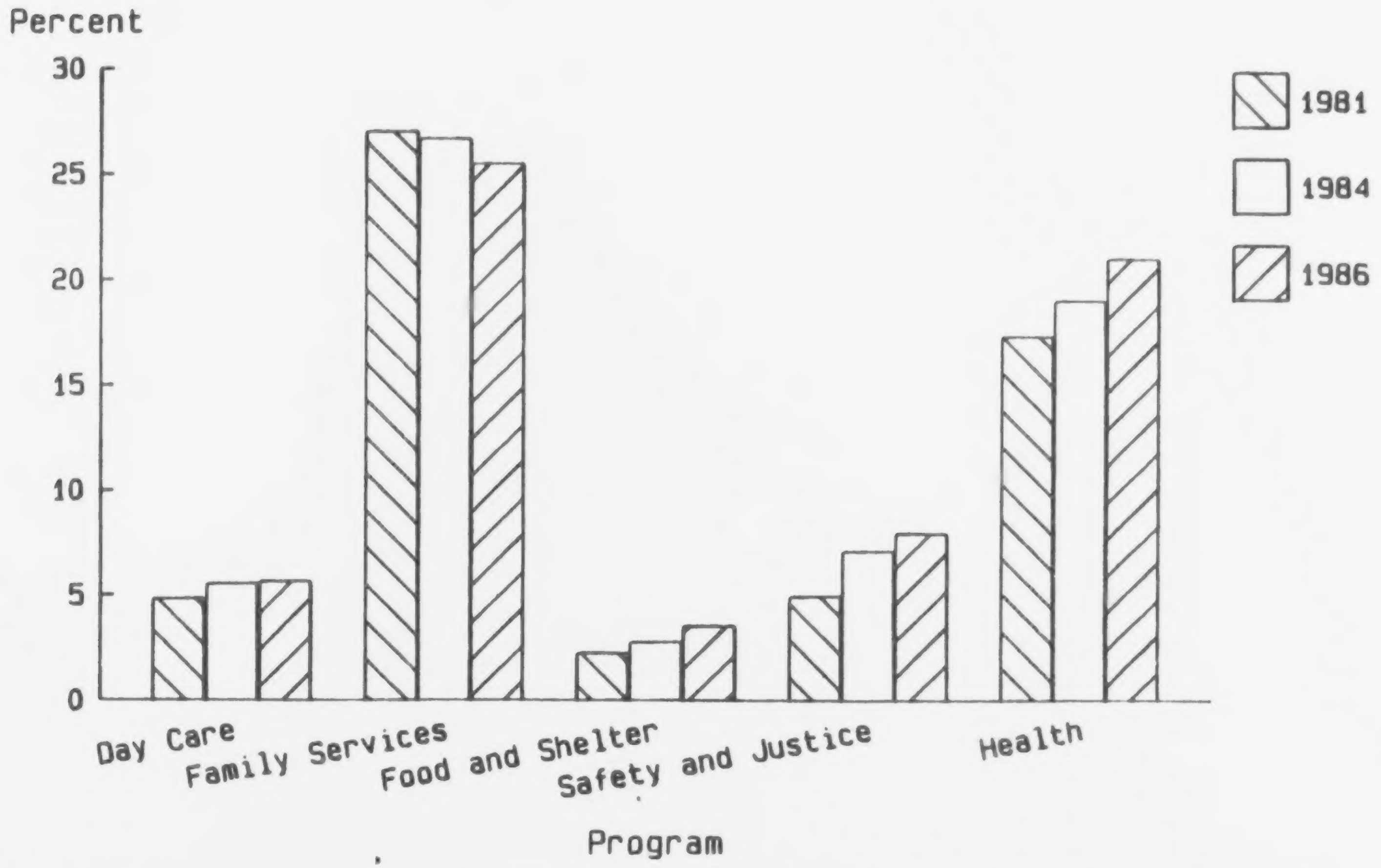
Figure 2

Sources: United Way of America
Profile of 1983 Allocations, Table 1
Fund Distribution Results, 1986, Table 1

Number of reporters 1981, 426; 1984-86, 415

Figure 3

Funds as a Percent of Total Annual Reported Program Allocations: 1981, 1984, and 1986



Program categories correspond to UWASIS II program service codes.
Data for 1981 represents Metros 1-4 only.

Sources: United Way of America 1981 and 1984 Allocations Surveys, and 1986 Fund Distribution Survey

NOTES

1/ The views presented in this paper are those of the author, and do not necessarily reflect those of United Way of America.

2/ The Nonprofit Sector Project has produced many noteworthy studies of the relationship of government to agency. The source for the figure cited is Salamon, Musselwhite and DeVita, 1986, Table 4.

3/ United Way of America, 1976. Russy D. Sumariwalla is the architect of the taxonomy.

4/ United Way of America, 1986. See Appendix D for the definitions of each program/service. In general, the categories are more specific than UWASIS II Goal Areas, but less specific than the six-digit coded categories contained in the volume.

5/ The total reported dollar figures, of course, vary. For 1981, they were $722.7 million; in 1984, $869.25 million; and in 1986, $1,070.2 billion.

6/ Since the survey historically contained a "miscellaneous" category, it has proved useful to examine agencies so coded for common names or themes. This examination has proved a useful impetus for introducing new categories to be tracked individually, as well as trends in emerging perceived needs.

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SECTION EIGHT:

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DONATIONS, LOCAL GOVERNMENT SPENDING, AND THE 'NEW FEDERALISM'

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Prepared for the 1988 Spring Research Forum
"Looking Forward to the Year 2000:
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The research described here has been supported by grants from the National Science Foundation and Yale University's Program on Non-Profit Organizations, with the latter providing sole support for this paper. A slightly different version of this paper will appear under the same title in Richard Magat, ed., Philanthropic Giving (New York: Oxford University Press (forthcoming). I would like to thank Paul DiMaggio and Richard Magat for comments on this paper, and Robert Inman, Thomas Reiner, Susan Rose-Ackerman, Julian Wolpert, Avner Ben-Ner, Steven Craig, Lawrence Lindsey, and Russell Roberts for their help on the underlying research.

I) Introduction

The nonprofit (NP) sector has long been recognized as a decentralized and pluralistic alternative to government for the provision of vital social services. Indeed, it is only in the last few decades that we have come to rely upon a governmental "safety net" to provide for the impoverished and disabled, and large-scale governmental support for the performing arts is of even more recent vintage. In light of the Gramm-Rudman amendment and philosophical objections to centralized solutions, this trend may reverse itself, and this paper considers the likely effects of a reduced federal role in social service provision.

The chief philosophic impetus for this retrenchment comes from proponents of the 'new federalism', who worry that centrally imposed solutions take insufficient account of local conditions and preferences, stifling experimentation and innovation. They worry about the potential for corruption and waste when power is centralized. Perhaps most importantly, they worry about the alienation of the citizenry when social problems are handled in a distant and centralized fashion. In their ideal world, competitive for- and NP organizations would make governmental solutions unnecessary, though they realize that some problems require federal solutions and some require local government solutions.

Thus, advocates of the new federalism tend to recommend a substantial reduction in federal expenditures (in the forms of direct expenditure, targetted grants, and revenue sharing) on social problems. They believe that expenditures on these problems will not necessarily decrease with federal support, for state and local governments and NPs can step into the breach. They hope that centralized services will be replaced in a pluralistic fashion, with an improvement in quality and a decrease in voter alienation.

NPs do provide a pluralistic alternative to government. Indeed, Burton Weisbrod (1975) has argued that in many cases the existence of NPs can be explained by dissatisfaction with majoritarian provision of public goods by local governments, which tend to provide the level desired by the middle (median) voter. This implies that 50% of the electorate would like to see less government spending (they are stuck) and 50% would like to see more. These undersatisfied voters supplement public provision by donating to local NPs providing similar services.

Despite the inherent desirability of this pluralistic alternative, the empirical underpinnings of the new federalist position are suspect. Will local government and NP expenditures rise in response to federal cutbacks? Will they rise sufficiently to replace the federal spending? This paper summarizes a technical paper of mine (Steinberg, 1987) which analyzes these questions.

II) The Theory of Crowding-out

A) Donations

The effect of government spending on donations depends on the underlying motivation of donors. Some people might give because they are unhappy with the level of some "local public good" and wish to raise that level. Here, we employ the economist's definition--a good is locally public if everyone in the community can enjoy its provision regardless of who does the purchasing (consumption is nonrival). An example of a public good is voluntary income redistribution, for many of the benefits of redistribution (such as a lower crime rate and a reduction in exposure to sorry scenes of poverty) accrue to each person in the community.

This motivation probably underlies some portion of those contributions that support income redistribution, civic improvements, medical research and other such causes, but it is doubtful that giving behavior can be explained by this factor alone. For one thing, the magnitude of giving is too great. In larger communities, the individual motivation to contribute is limited in part by each donor's fear that his or her contribution would enable others in the community to reduce or eliminate their contributions and take a "free ride." In this setting, donations per capita are vanishingly small in all but the smallest communities (Andreoni, 1986 or Kingman, 1987). When government spending is introduced in such a model, the predictions become even less realistic. Warr (1982) and Roberts (1984) have shown that when the only motive for giving is to augment the provision of a public good, there will be dollar for dollar crowdout--that is a one dollar increase in government spending is entirely neutralized by the response of other donors. If government spending is great enough, donations would be driven to zero and can fall no further, implying that government spending is only useful past this point. Thus, in such a world, we wouldn't expect to see government spending and charitable donations coexisting. Since free-riding behavior implies that donations alone will be too small in that voters would unanimously support an increase if everyone were required to do their share (as occurs with coerced government taxation), and coexistence is irrational, we'd expect observed donations to be zero. Clearly, they are not, so this model of donor motivation is inadequate.

A second donor motivation is the receipt of private benefits in return for one's donation. These benefits may be something tangible (like a front-row seat or an alumni magazine), intangible but observable (prestige, friendship, respect of ones boss) or strictly internal (the 'warm glow' of having done the right thing). In my model, I allow both sorts of motivation, and the two are inextricably intertwined. A donor is unlikely to obtain large satisfaction from the act of giving if needs are already being met by governments or other donors. NPs are unlikely to offer large private-good rewards unless their needs are acute.

Rational donors implicitly compare the additional (also known as 'marginal') benefits forthcoming from a marginal donation with the marginal costs. Any time these marginal benefits exceed the marginal costs, the donor would be better off if he or she increased their donation. Utility is maximized when marginal benefits equal marginal costs. This is true because marginal benefits typically decline as consumption of any good increases (at least past some point). The first dollar of contribution provides larger additional benefits than the last dollar for the same reason that the first ice cream cone adds more happiness than the fifth cone. With diminishing marginal benefits, a donor who set marginal benefits equal to marginal costs would break even on the last dollar contributed and come out ahead on every earlier dollar.

The cost of giving is simply the dollar value of the donation, so that the marginal cost is about $1 (tax deductions would lower this cost, while administrative waste would raise it). Figure 1 illustrates the donor choice. If private benefits were the only donor motivation, then this choice would be independent of government spending, but in general, the location and shape of the schedule of marginal private benefits depends on both the giving of others and government spending. If spending by others were to rise, and were viewed as an imperfect substitute for one's own donation, then the marginal benefits schedule would fall, as would the optimal personal donation. This phenomenon is called "simple crowdout."

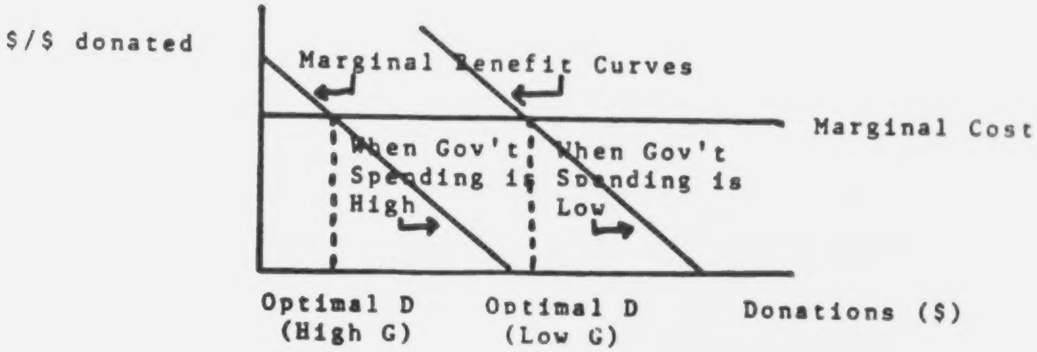

Figure 1: Effect of an increase in government spending on a single donor when donations and government spending are felt to be imperfect substitutes for each other by the donor

I've illustrated the most common case, but there are several reasons to expect to donations to occasionally move in the opposite direction (which I call 'negative simple crowdout'). Rose-Ackerman (1981), analyzing federal expenditures in the form of grants to NPs, noted that donors might view the grant as a signal that the recipient organization is especially efficient and/or meritorious, and respond positively to this "seal of approval." Alternatively, grants may be accompanied by strings that affect the ideology of the organization so as to make it more attractive to smaller donors, e.g., if it engages in less controversial activities. Third, grants may fund services which are complementary to the donative services. For example, if government funding built a symphony hall, donations for the symphony's operating budget will be encouraged. Finally, grants may be made on a matching basis, lowering the effective price of giving and stimulating an increase in donations.

When governmental expenditure takes the form of direct provision (i.e., a veteran's hospital, a public university, or Aid to Families with Dependent Children), there is a presumption that private donations will fall but this is not necessarily so. The presumption stems from the so-called substitution effect, where the meeting of related needs by government spending reduces the marginal benefit of donations to the donor. In addition, governmental spending increases may be accompanied by tax increases, which would decrease after-tax income and hence donations. This will be denoted the tax effect.

However, government spending could cause donative increases for three reasons. First, the substitution effect would run in the opposite direction when donations are complementary to the governmentally-provided service. Second, if tax increases are achieved by an increase in marginal income tax rates, then the value of the tax deduction for charitable donations will increase for itemizers. This would reduce or even reverse the tax effect. Third is a perverse 'income effect'[1]. When total social service provision is viewed as inadequate by a voter (accounting for the tax increase necessary to increase such spending), then increased spending acts like increased income (since they can now consume more of something they like), encouraging a donative increase. This acts in the opposite direction from the substitution effect. Conversely, the substitution effect is amplified by the income effect if government spending is viewed as excessive, for then a government increase subtracts from real income resulting in lower donations.

Combining the substitution, tax, and income effects, we expect partial crowdout--total donations will fall, but by less than the governmental increase. Within this model, crowdout is perfectly symmetrical, so we expect that governmental decreases will be only partly made up by donative increases. The prediction that crowdout will be partial represents my judgement as to the likely size of these competing effects, and cannot be established on purely theoretical grounds. My judgement is strengthened, however, by consideration of a fourth and final factor--the feedback effect.

Donors respond not only to government spending, but to other donors. The three effects described above consider only the direct reaction to government spending increases by each donor.

But, if each donor cut back in direct response to the governmental increase, then each would readjust in light of cutbacks by other donors, moderating the original impetus[2]. The feedback effect could work to amplify the original impetus only if donors wished to copy each other in some sort of herd mentality, which I think is a less common situation. Table I summarizes the four effects.

Table I: Effects of a Direct Governmental Expenditure Increase on Related Donations

Name of Effect	Possible Impacts on Donations	Probable Impact
1) Substitution	Reduction (If governmental expenditures are a substitute) Increase (If governmental expenditures are a complement)	Large Reduction
2) Tax[a]	Reduction (If marginal rates are unchanged) Unclear (If marginal rates are increased)	Small Reduction
3) Income[a]	Increase (If governmental expenditures are not excessive) Decrease (If governmental expenditures are excessive)	Small, direction unclear
4) Feedback	Decrease Aggregate Impact (If donations of others are a substitute) Increase Aggregate Impact (If donations of others are a complement)	Diminish Aggregate Impact
5) Total		Moderate Reduction (Partial Crowdout)

Note:

[a] In both these cases, we assume that desired donations increase with income, all else constant. Exceptions to this assumption are quite rare.

Several studies have been done of simple crowdout. None of them is perfect, for there are serious problems with existing data sets and unresolved problems of statistical methodology. Nonetheless, they are collectively persuasive that crowdout does occur, that the extent of crowdout varies with the type of service provided, but is generally partial. Table II summarizes these studies.

B) Local Government Spending

Local government expenditures must generally accord with the wishes of the electorate[3], so it is safe to predict the average behavior of governments from the preferences of median voters. These voters compare the marginal costs and benefits of local government spending. If marginal benefits exceed (are less than) marginal costs at some initial level of government spending, then voters would ask for a governmental increase (decrease). In equilibrium, voters wish a level of governmental spending which equates marginal costs and marginal benefits. In this case, however, calculation of the marginal cost and benefit schedules

TABLE II: EMPIRICAL STUDIES OF SIMPLE CROWDOUT

Study	Crowdout Parameter[a]	measure of government spending	measure of donations
1) Abrams and Schmitz (1978)	$-0.236^{b,d}$	federal expenditure on health, education, and welfare	Deductions on U.S. Federal Income Tax Returns
2) Reece (1979)	-0.011 to -0.100	AFDC + old age assistance + aid for disabled/recipient	Various from National Survey of Philanthropy (U.S.)
3) Paquè (1982)	-0.06 to $-0.35^{c,d}$	social service public expenditures	Deductions on German (F.R.G.) Federal Income Tax Returns
	0.118^{c}	health and recreation public spending	
	0.11 to $0.31^{c,d}$	cultural affairs public spending	
4) Amos (1982)	-0.002 to -0.462^{d}	total transfer income; AFDC ; public welfare payments	Deductions on U.S. Federal Income Tax Returns
5) Steinberg (1983)	-0.001 to -0.003	intergovernmental grants for recreation	Local United Way Allocations to Specified Service (U.S.)
	0.004 to 0.009^{d}	intergovernmental grants for hospitals.	
6) Jones (1983)	-0.015 to $-0.016^{b,d}$	central and local government spending on social services and housing	Family Donations from Family Expenditure Survey (U.K.)
7) Schiff (1985)	-0.66^{d}	local government expenditures	Various from National Survey of Philanthropy (U.S.)
	0.046^{d}	state noncash welfare spending	
	-0.058^{d}	state cash assistance	
8) Abrams and Schmitz (1984)	-0.30^{d}	state and local social welfare payments/$1000 personal income	Deductions on U.S. Federal Income Tax Returns
9) Steinberg (1985)	-0.005^{d}	central and local government spending on social services and housing	Family Donations from Family Expenditure Survey (U.K.)

Notes: a) Change in donations caused by a $1 increase in government spending
b) Calculated from reported elasticities and available data.
c) Elasticity (relates percentage change in government spending to percentage change in donations). Conversion to parameter not possible.
d) Reported coefficients different from zero at .05 or better. In some cases, the crowdout parameter is a nonlinear function of reported coefficients and significance tests were not performed for the former.

is more complicated. The marginal cost expenditures is chiefly an increment to taxes. This cost is reduced for itemizers under current tax law because local taxes, like donations, are deductible from federal taxes. The cost is increased if local government is an inefficient provider of services.

Two factors affect the marginal benefits of local government expenditure. First is the leverage effect--a vote to increase governmental expenditures is a vote to increase the (mandatory) contributions of all other households in the community. Second is the crowdout effect--when government spending goes up, private donations for related purposes respond. We have argued that crowdout is generally partial. This means that government spending would still have marginal benefits, but they would be smaller since decreases in donations partly negate increases in government spending.

In general, communities with a greater crowdout effect will have smaller local government expenditures[4]. Similarly, within any community, government spending will be larger on those services with smaller crowdout effects, all else equal.

C) Intergovernmental Aid to Local Governments

Local governments receive transfer payments from other levels of government (I will refer to them generically as "grants") in the forms of categorical assistance (a grant targetted to a specific purpose) and general assistance (such as revenue sharing). Some grants are unconditional, while others have a matching requirement. Grants may be expected to alter both private donations (via simple crowdout) and local government spending (via simple government crowdout, explained below). In turn, induced changes in donations have feedback effects on local government spending while induced changes in local government expenditures have feedback effects on donations. The ultimate impact on total expenditures for the public good is denoted "joint crowdout."

Simple government crowdout has been analyzed by a number of authors (Inman 1979). The extent of such crowdout depends crucially on the details of grant administration. The simplest case to analyze is general non-matching assistance such as revenue sharing. This type of grant induces only income effects, for it is analytically equivalent to an increase in the average income of the community. The income effect here is almost certainly positive, since the cost of a grant to local taxpayers is essentially zero so no voter will be oversatisfied. Thus, some portion of the grant will increase local government spending while the rest will finance local tax reductions, an outcome I call partial simple government crowdout.

Matching requirements cause price as well as income effects. In effect, the matching rate acts like a reduction in the price of the social service when provided by a local government. The net result is that simple government crowdout by matching grants is numerically smaller, and may even go negative (that is, local taxes may increase to finance a more than proportionate increase in local spending).

Theoretically, targetted and general grants should have the same effects, as the grantor cannot distinguish what local government spending would have been in the absence of the grant. As long as spending on the targetted program is as large as the grant, the community can plausibly appear to be spending the entire grant on an increment to the targetted program when in fact it is replacing intended spending from own resources with grant spending. Theory falls short here, as a large body of evidence suggests that targetted grants produce many times larger effects than community income increases. This effect is called the 'flypaper effect', since money seems to stick where it hits, and has been explained using a richer model of the political process than the one employed here (Craig and Inman, 1986).

Grants affect both private donations and local government. In turn, donations and local government expenditures respond to the induced changes in each other--joint crowdout. Tracing the web of causalities I have shown elsewhere that, for non-matching grants:

1) Partial simple crowdout of donations generally implies partial joint crowdout[5]. Thus, total spending will rise and fall with intergovernmental grants, but by a smaller amount than the grant.

2) When there is negative simple crowdout, joint crowdout is likely to be partial, but zero or negative joint crowdout are also possible.

3) When there is super simple crowdout, local government spending on the service will cease.

4) The portion of local government spending financed by local taxes will fall in response to a grant, though total local government spending (including the grant) will rise. Donations may rise or fall in political-economic equilibrium regardless of whether simple crowdout is partial or negative.

Some of these conclusions are altered when grants are of the matching variety. With matching grants, the tendency towards partial joint crowdout is reduced or reversed, and total spending may go up by an amount which exceeds the grant.

D) Some Evidence

It is extremely difficult to estimate the size of joint crowdout. For one thing, in order to preserve confidentiality, most surveys of giving do not record the location of the respondent, making it impossible to correlate giving and local government spending. For another, the theory has not been developed enough to allow us to take sufficient consideration of provision of social services financed by local government user fees or provided by for-profit firms. Nonetheless, it is important to produce the best estimates possible.

In ongoing work, Lawrence Lindsey and I have attempted to circumvent the first problem by assembling a data set which reports itemized donations by taxpayers in each of six income classes, 50 states, and three years. Using multiple regression analysis, which, when successful, removes the confounding influences of the many things changing at once in the real world to focus on joint crowdout, we have produced some preliminary estimates (Lindsey and Steinberg, 1988) which we hope to refine further.

We had three measures of donations, three measures of state spending, and two measures of federal grants. Seperate estimates were produced for donations of cash (CASH), of assets (ASSET), and their total (CHAR). The broadest measure of state spending, S1, included per-capita state and local spending on elementary and secondary education, higher education, welfare, health and hospitals, housing and urban renewal, and natural resources, parks, and recreation. This included virtually all facets of state activity which might plausibly be related to private donor activity. S2 included state and local spending on all of the above except housing and urban renewal and natural resources, parks, and recreation. S3 included only spending on higher education, health, and hospitals, which correspond to the two largest recipient groups (after religion) of private philanthropy. F1 includes total per capita federal transfer payments to state governments, while F2 includes only transfers targetted to education and welfare programs.

Table III summarizes our results. The broader measure of federal grants, F1, appears to cause donations to fall by about 54¢ on the dollar after all feedbacks have played through, and to cause state spending (including the grant) to rise by between $1.78 and $0.34, depending on the measure of state spending. If, as the authors contend, S3 is an overly narrow measure of state spending, then the federal grant causes an increase in state spending from its own resources (i.e., excluding the grant) of between 52¢ and 78¢, which is consistent with the flypaper effect found in other studies. It is this flypaper effect which causes donations to fall by so much--donations respond not only to the increase in federal spending but also to the matching increase in state spending. The implied value of simple crowdout (holding state spending constant) is a decrease of between 16¢ and 19¢ per dollar, which is consistent with the values estimated in the previously cited studies.

The narrower measure of federal grants, which includes only transfers that seem related to donations, appeared to have a

Table III: Effect of a $1 Increase in Federal
Transfer Payments on:

Dependant Variable	Using F1	Using F2
CASH	-$0.4593	-$0.9832
	(0.1703)	(0.3026)
ASSET	-$0.0839	-$0.2941
	(0.0544)	(0.0982)
CHAR	-$0.5432	-$1.2761
	(0.1909)	(0.3392)
S1	+$1.7845	+$2.3754
	(0.1426)	(0.3494)
S2	+$1.5213	+$2.2173
	(0.1338)	(0.3061)
S3	+$0.3485	+$0.0483
	(0.0738)	(0.1553)
CHAR + S1	+$1.2413	+$1.0993
CHAR + S2	+$0.9781	+$0.9412
CHAR + S3	-$0.1947	-$1.2278

Note: Standard error in parentheses beneath parameter estimate.
Source: Lindsey and Steinberg, 1988.

larger effect on all variables. Now, state spending is found to rise by between $2.22 and $2.38 per dollar, inducing much larger joint crowdout of donations of $1.28 per federal dollar. This difference appears to be primarily due to the largest flypaper effect, as the implied value of simple crowdout of CHAR is about the same--a drop of 17¢ to 18¢.

Overall, federal spending appears to be especially productive as long as S1 or S2 is viewed as the appropriate measure of state spending. Total spending rises by between $0.94 and $1.24 for each dollar spent by the federal government. Conversely, federal cutbacks will not be made up by the combined response of state governments and donations--indeed, they may amplify, not ameliorate, the impact of the cutback.

III) Summary

One of the main tenets of the new federalism is that local governments and nonprofit organizations will increase their expenditures on social services in response to federal cutbacks. While the case for federal cutbacks does not rest entirely on this empirical assertion, this relevant issue is examined on the theoretical level.

The relationship between government spending and private donations is not simple, but theory suggests that there will usually be partial simple crowdout--that is, that government expenditure increases (decreases) are partly neutralized by donative decreases (increases). A number of studies, each flawed but cumulatively persuasive, are cited to show that simple crowdout is usually partial, typically running between 1/2 and 30 cents on the dollar. This suggests that when a local government reduces its provision of social services, it cannot count on the nonprofit sector to replace a very large part of these services, although some replacement will occur.

When federal grants for social service provision are cut back, local donations and government spending respond both directly and to the induced changes in each other. If total spending goes up by less than an increment in intergovernmental aid, we say that joint crowdout is partial. Partial joint crowdout is most commonly expected on theoretical grounds, but theory does not rule out other outcomes. Currently available data sets do not, however, allow easy confirmation of this conclusion, but preliminary estimates suggest that joint crowdout is near total. Thus, federal cutbacks will not be made up by the other sectors.

NOTES

[1] Though I have used the terms "income" and "substitution" effects, this usage is not equivalent to the traditional usage of these terms in economics. Traditionally, these terms are reserved for the effects of a price change on desired purchases of a good. In this case, we are regarding the effects of a change in a quantity-constrained good (that is, a good whose purchase is not under the control of the donor) on desired purchases of a related good (donations) which is under donor control. Mackay and Whitney (1981) showed that the impact of a change in a quantity constraint can be broken down into effects that are analogous to those resulting from a price change, which they called income- and substitution-like effects.

[2] The feedback is accounted for in the companion piece by calculating the change in the Nash equilibrium allocation. See any textbook on game theory such as Friedman (1977) for a discussion of the Nash equilibrium concept.

[3] There are a number of reasons why local government expenditures would depart from the wishes of the electorate. Governmental bureaucrats provide information to voters, and this information can be manipulated to sway elections. Preferences of voters may be such that there is no stable voting outcome--just continuing political cycles. Voters may be unmotivated to gather information necessary for their decisions, voting on whims or images. For a review of these and other problems, see any standard political economy text such as Atkinson and Stiglitz (1980). Nonetheless, the median voter model seems to have good predictive power (Inman, 1978) and may serve as an adequate simplification of reality for our purposes.

[4] There is a perverse income effect here as well which could (in theory) reverse the relation between the crowdout parameter and local government spending. In practice, it is exceedingly unlikely that this income effect would be large enough to reverse the conclusion of the text.

[5] Exceptions are possible, but sufficient conditions to insure this result are that all goods are normal, the choice set is convex for the decisive voter, political-economic equilibrium is interior, and donations are locally linear.

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WORKING DRAFT

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NEW APPROACHES TO FINANCING NONPROFIT ORGANIZATIONS: THE ROLE OF LENDING

by

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NEW APPROACHES TO FINANCING NONPROFIT ORGANIZATIONS: THE ROLE OF LENDING

Overview

This paper reviews the possibility of extending the program investment approach--utilized, to date, primarily in the areas of housing and economic development--into human services. It address a number of key questions: How useful would it be to designate special funds to lend to nonprofit agencies to assist them in developing new or restructured human service programs? Could borrowed funds feasibly be repaid either from existing cash flows or from new financial packages that could be put together? Would loaned funds help assisted organizations establish more innovative and effective programs? Would lending funds provide incentives for more business-like performance by the nonprofit sector? Would such programs require establishing special financial intermediary mechanisms in which foundations and corporations could invest? Answers to these questions could help provide important new directions for the human service system and those who help finance it.

The Changing Human Services System

Both for-profit and nonprofit service providers have important roles in the U.S. human service system. Over the past 20 year, the role of the nonprofit sector has broadened substantially as new areas of special need have been identified and sources of funding made available. At the same time the boundaries between the nonprofit and for-profit sectors have begun to blur. Traditionally, nonprofits have operated in fields where ethical and financial considerations constrain private firms. Such categories include family planning or the provision of emergency shelters for abused spouses and children. This is the historical pattern of nonprofit operations: responding to needs of a sensitive or controversial nature and depending largely on local public funding and charitable contributions, rather than government reimbursement. But, shifts in sources of financing have allowed the for-profit sector to develop a market in some areas where the nonprofit sector was once dominant. In addition, economic pressures have encouraged nonprofits to adopt more businesslike and enterprise-oriented practices.

Health care services illustrate the growing mix of nonprofit and for-profit providers in human services. Since 1965, Medicare has played a central role in transforming the nonprofit, charity-based hospital system into a profitable market. Since 1965, for-profit hospitals have competed with nonprofits for the publicly financed and fee-for-service market. Although debate continues over which sector provides the best care at the best price, there is no longer much doubt that as long as there is medicate or private health insurance there will be both for-profit and nonprofit health care providers, with the nonprofit sector focusing on low-income patients.

In education and training, the broadening mix of individual, corporate, and public reimbursement has maintained a mix of nonprofit and for-profit providers for all segments. The market is likely to remain mixed indefinitely, as public and private needs and programs (such as the Job Training Partnership Act) evolve, although nonprofits may gradually be pushed into serving those least able to help themselves.

The mixed nature of today's human service system raises several concerns. First, there may be some forms of human service for which the lack of market makes nonprofits the only feasible provider. Second, there are areas of human service in which participation by profit-motivated providers may never be ethically permissible (e.g., organ banks for transplants). How can such nonprofit providers be assisted to continue operation and to upgrade their programs to meet changing needs? Many will need assistance in redesigning the ways they do business if they are to survive. Third, new human service businesses to meet expanding needs (e.g., child care) may need to be fostered in some areas.

The Need to Finance Design Change

Changes in the structure of the economy and in the demographics of communities have created new needs and opportunities for human services providers over the past decade. In addition to the blurring of boundaries between the fields of nonprofit and for-profit operation, new understandings have created pressure for redesign in the nonprofit sector so that it remains competitive with the for-profit human service system.

Some of the most striking examples of how these forces are operating can be found in the area of health care. Federal and state government concern over escalating medical costs, combined with employer and insurer cost containment concerns, have led to a dual assault on the hospital-based health care system. The introduction of the diagnostically related group (DRG) Medicare reimbursement system and the private sector's pursuit of preferred provider organization (PPO) agreements have led hospitals to undergo substantial reorganization. Beds have been eliminated, lengths of stay have been shortened, and employees have been laid off. This process, however ungraceful, has further led to a redesign of the general health care system. Both for-profit and nonprofit hospitals are now competing on prices and services, and are diversifying to expand market share. It is not clear whether the best health care is being provided and whether the poor are being served. Nevertheless, less expensive forms of outpatient care, prepaid health care, and community-based long-term care are becoming more widely available. Similar forces, on a smaller scale, are affecting other human services.

In the field of education and training, economic restructuring has created skill gaps that will have to be filled--from the basic literacy-numeracy level through graduate studies and specialized vocational training. New employer-based, proprietary, vocational, and public-school/community-college education and training programs are emerging, or are being sought by business and government to ensure that the economic recovery has the appropriate labor force it requires. At the same time, the chronically unemployed and long-term displaced workers are being left out of many programs. Thus, there is clear need to redesign education and training systems both to meet changing requirements and to ensure equity for those who need help most.

As these examples show, the pressure to change the systems of human service provision is mounting. Today the question of preserving the nonprofit sector for its own sake matters less than the need to foster adaptation of existing nonprofit services to the new environment, or to help establish new nonprofits to meet needs the market does not address.

Recent Experience

A number of recent studies have examined the potential for using program related investments to enable innovation in the nonprofit sector through research projects and consultations. Several early projects evaluated needs for financial innovation in specific service fields such as child care, adult day health care and development of health care insurance for employees of small businesses. Other studies evaluated business opportunities that would serve specific need populations, such as the older adult. One specific study was carried out in 1987 conducted under the aegis of a National Steering Committee of local United Way executives, managed through the United Way of America, with assistance from a project study team consisting of representatives from the local United Way organizations in the test cities of San Francisco and Cleveland, United Way of America, SRI International, and Mitchell Sviridoff Associates.

The research that has been carried out has examined four critical questions that must be answered in determining the feasibility of using lending more in the area of human services:

- Could the development of human service lending programs result in a new source of capital that can promote innovation and adaptation in the human service sector?
- Could human service agencies develop programs that could generate sufficient revenues to repay loans?
- Would the foundation and corporate philanthropic community support initiatives in this area?
- What would be he benefits and drawbacks of establishing new intermediaries to promote investment in the human services?

Answers to these questions come from experiences in communities across the United States, as well as through interviews with foundations and corporations.

The Impact of Program Investment on Innovation in Service Delivery

Examinations of an array of nonprofit service enterprises in recent years reveals three key findings concerning the potential impact of social investments on the delivery of human services.

First, the use of a loan mechanisms would be instrumental in creating a new management perspective among human service agencies. Many agencies have the internal administrative capacity--in terms of financial and planning expertise and management systems--required to take on a loan. However, the use of loans would require that human service agencies take a more market-oriented approach to the services that they provide. For example, in providing case management services for the mentally ill, or establishing an adult day health care center, an agency must be able to estimate how may clients will be Medicaid eligible, what percentage of costs will be reimbursable, how many clients can afford to pay the fees themselves (if any), and how many need to be subsidized through some alternative source. Such business-like approaches are critical in developing a loan project because agencies must have firm projections of their costs and revenues to develop a cash flow analysis that can demonstrate their capacity to repay a loan.

The readiness of an agency to think about their client population as a highly varied market, and to recognize that sources of reimbursement may comprise a diverse array of revenue flows is central to both innovation in design of programs and their ability to repay a loan. In the case of an adult day health care facility, for example, a program may need to define its market in different ways. Clients could include frail low income older adults, older workers with occupational rehabilitation needs, dependents of working adults, and recuperating independently living older adults. Reimbursement sources could include Medicaid, but also Medicare, private insurance, contracts with other health care agencies (hospitals, HMOs), as well as fee for service based on a sliding-scale. It is in this area of developing marketing and feasibility studies that a financial intermediary will most likely need to provide technical assistance and grants to nonprofits.

SRI findings suggest that there is increasing sophistication among providers in targeting client markets and in defining reimbursement streams that enable programs to break-even while meeting their service mission. Competitive pressures have encouraged improved management and innovation in the design of human services. Loan programs would reinforce this trend.

A second key finding is that loan funds would be able to meet the capital needs of some but not all nonprofit human service agencies. In some cases, the dynamics of the reimbursement system for a particular service will not permit repayment of a loan. In others, the notion of borrowing money simply does not fit within an agency's organizational culture.

Finally, a third finding is that the availability of loan dollars could result in important benefits in the delivery of services in communities where loans are made by enabling the development of innovative programs that meet existing human needs in ways that provide pay-backs to agencies. Clearly, providers are showing increased sophistication in recognizing alternative ways of delivering human services that might be suitable for program related investment. Among these are: nonprofit service businesses that offer financial management services for frail older adults living in the community that prevent their becoming custodial or public guardian cases; home equity conversion programs that can generate fees from banks for serving as a neutral party in screening and preparing equity conversion loans; caretaker placement services that match persons seeking work with daily or live-in care taker roles for the disabled or frail; insurance cooperatives that provide health insurance for employees of small businesses. There is an emerging human services entrepreneurship that can be encouraged by the availability of what might be considered to be "social venture capital" to finance start-ups or diversification by human service agencies.

Foundation and Corporate Support

Another fundamental question that appears to have been answered in establishing the feasibility of mechanisms for making loans to nonprofit organizations is whether foundations, corporations, government, and other funders will be willing to invest in providing such loans. Each of these three types of potential funders will have different motivations for lending to human service agencies. For example, the use of loans can provide foundations with a means to provide funding that will allow a program or agency to become self- supporting, without resulting in a continuing drain on the foundation's budget. In addition, loans can make a foundation's dollars go further, can potentially leverage other sources of funding, and can help to build new management capacity in the agencies that the foundation supports. However, it is important to note that although smaller local foundations are also interested, few of them have had experience with the concept of program related investment (PRI). This is largely because of the complexity of PRIs, both in terms of understanding the benefits of the PRI to the foundation, and of the staff expertise required to make PRIs.

Table 1 presents some of the barriers and incentives that foundations generally face in making PRIs.

Table 1

INCENTIVES AND BARRIERS TO PROGRAM-RELATED INVESTMENTS BY FOUNDATIONS

Incentives

- Recyclability--Because loaned funds come back to the investor, they can be invested again.
- Leverage--By providing a portion of the needed financing, PRIs can often leverage additional corporate or foundation funding.
- Tax Benefits--PRIs and their associated costs are counted toward the qualifying distribution, but not as part of a foundation's asset base.
- Flexibility--PRIs can be funded out of a community or corporate foundation's corpus or its grant budget, and can be used in place of or in conjunction with a grant.
- Capacity Building--PRIs can help to increase the capacity of recipient organizations by stimulating the development of new planning, managerial, and financial skills.

Barriers

- Lack of Expertise--Many foundations and corporations are not large enough to develop the needed staff capacity.
- Income Generation--Some foundations have a conceptual difficulty with making money on their charitable giving.
- Performance--Many foundations are concerned about the impact that a low-interest, high-risk loan will have on their investment performance.
- Legality--Although IRS regulations provide a specific exemption, some foundations fear that the use of PRIs could violate the prudent man rule.
- Perceived lack of Financial Strength--In some cases, foundations assume that only the the largest foundations have the financial capacity required to make PRIs.

Corporations will have slightly different incentives for lending to human service agencies. Firms in industries such as insurance and banking often have access to large amounts of funds that can be loaned out but not given away. These funds are separate from those that might be set aside for corporate contributions. In some cases, these corporations count the interest forgone in making a social investment at concessional rates toward their internal budget for corporation contributions. However, regardless of how these loans are treated internally, the use of loans can allow corporations to support their social and public relations goals of assisting the human services sector in their community without significant costs. In addition, the fact that the use of loans can promote a more businesslike approach to service delivery will be very attractive to corporate lenders.

Finally, the government also has an interest in promoting innovation, fiscal accountability, and a new management perspective in the human service sector, which it is largely responsible for supporting. Increasingly, Federal and state programs, like Community Development Block Grants, have been utilizing loan mechanisms.

Need for New Financial Intermediaries

One important issue is the extent to which new mechanisms need to be created to serve as financial intermediaries between funders and recipient agencies. Intermediaries can not only allow funders to achieve their programmatic goals of supporting innovation in the human service sector, but can allow investors to eliminate some of the administrative and information costs and the risk that they face in making an investment. However, the development and use of an intermediary has also raised certain concerns among potential investors; these must be understood in designing an effective and attractive intermediary.

Overall, the use a financial intermediary could result in two important benefits to investors:

- More Efficient Achievement of PRI Objectives--Because the financial intermediaries could have a highly skilled and specialized staff, they will be better able to promote innovation and a new management perspective among recipient agencies than would a foundation itself.

- Reduced Barriers to Investing Through PRIs--Financial intermediaries, can reduce the administrative costs and staff requirements needed to make a PRI, because investors need only make one loan to the intermediary, rather than several, more risky loans to individual agencies.

At the same time, some potential funders raised the following issues as potential drawbacks to establishing future financial intermediaries for program related investments. These concerns can be successfully addressed if the future financial mechanisms are properly structured and understood. The drawbacks mentioned were as follows:

- Replacement of Existing Funding Sources--Some potential investors have been concerned that rather than opening up a new stream of funding, new financial intermediaries might simply displace grant funds with loan funds; thereby diverting money from the most needy organizations to those that could sustain a loan. It is important to note, however, that experts in the field strongly believe that the large percentage of PRI funds represent new, rather than already existing, charitable dollars.

- Loss of Control Over Funding--Some foundations are concerned that they would lose control over the types of programs that they assist if they invested in an intermediary rather than directly in agencies. Financial intermediaries are likely to develop unique portfolios and specialties in lending to specific human service providers over time. As they gain experience they may broaden their capabilities and ability to lend effectively. Financial intermediaries could, as do banks and investment organizations, have specific concentrations that reflect their sponsor's interests. However, successful financial intermediaries are more likely to have pluralistic lending practices that reflect the quality and capabilities of the human service agencies themselves--including their ability to define a market that needs to be served, rather than specific themes.

Prospects for the Future

Studies by SRI and others have found that the establishment of a financial intermediaries to provide pools of loan money at below-market rates, could improve both service delivery and management in the human service sector. This work has also found that although few foundations have made PRIs in human service agencies, there are strong incentives for them to make PRIs now, as public resources for human services diminish, competition between providers increases, and need for innovation to meet special needs expands. The prospects for creation of new financial intermediaries to provide loans to nonprofit organizations appears good both because potential investors are discovering the value of program related investment and because human service providers are entering a period of enhanced entrepreneurship. Social investment mechanisms will be an important force in bringing program-related investments to the human service sector. Efforts to study the potential for these mechanisms has aroused interest on the part of national foundations and the federal government, as well as local foundations and corporations nationwide.

Moving ahead toward the establishment of new financial approaches for providing loans to nonprofit human service organizations would seem to be worthwhile. The availability of loan funds can effect both the ability of human service agencies to meet needs and their management capacity. At the same time, PRIs represent a growing yet largely untapped resource that could be drawn out through the establishment of a financial intermediary. By making the concept of lending to nonprofits a new business practice, the evolution of human service providers towards a more innovative, entrepreneurial organizations that better serve their clients will be enhanced. The social investment concept is still relatively new. There is a need for leadership both foundations, corporations, and the nonprofit organizations in bringing this new stream of funding into the human service sector.

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FINANCING NONPROFIT ORGANIZATIONS:
SALES REVENUE AND COMPETITION WITH PRIVATE ENTERPRISE

by

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This paper draws heavily from Chapter 6 of my forthcoming book, The Nonprofit Economy (Cambridge, Massachusetts: Harvard University Press, April 1988).

Nonprofit organizations rarely survive on donations alone. In fact few nonprofits even receive a substantial portion of revenues from donations. Some 38 percent of tax-deductible nonprofits received 10 percent or less of their revenues from donations; half received less than 25 percent from donations. At the other end of the spectrum, 21 percent of the organizations depended very heavily on donations, receiving more than 90 percent of their revenues in this form. Nonprofits are typically involved in a variety of fund-raising markets to make up the balance of revenues.[1]

Nonprofits increasingly encounter the proprietary sector of the economy as they pursue other sources of revenue. Small businesses particularly resent nonprofits' for-profit endeavors. Responding to numerous complaints from the small business community, Frank Swain, the Small Business Administration (SBA) Chief Counsel for Advocacy, said "Small private businesses are laboring under a tax code which taxes them but not some of their competitors--nonprofit organizations doing business for profit."[2] Increasingly the SBA and various industry groups within the small business community refer to nonprofits as "unfair competition."

This criticism of nonprofits combine both factual and normative issues. Is there substantial competition between nonprofit organizations and proprietary firms? Is the competition growing? What forms is it taking? Is such competition "unfair?" What should be the limits on what nonprofits may do to raise revenues? And even if the competition is unfair to the proprietary firms, is it inefficient or otherwise undesirable from a society-wide point of view? Only if it is unfair should public actions be taken to restrict the inventiveness of nonprofits in their search for new activities, markets and resources.

Competition

Supporters of both the nonprofits and the proprietary organizations agree that cutbacks in federal funding (beginning around 1980) have led an increasing number of nonprofits to seek new revenue by engaging in profit-making activities and the two forms of institutions have come into growing conflict.[3] A community group in Milwaukee, for example, has purchased a launderette in hopes of generating profits which can then be used for its community welfare activities.[4] Other for-profit endeavors of nonprofit organizations include a commercial weatherization and home improvement company, a food-management service for hospitals and schools, a restaurant,[5] a construction and home improvement company, a commercial greenhouse business,[6] and even a national for-profit development company that builds festival marketplaces in smaller cities.[7] Even public television, its government funding having been sharply cut, has resorted to dramatically new measures for raising revenues.[8] A recent book has the intriguing title Enterprise in the Nonprofit Sector.[9] That title includes two words that many people have traditionally regarded as contradictory. "Enterprise" and "nonprofit" are no longer contradictory, however. "Sixty-nine percent of the organizations we surveyed have given birth to new [profit-making] enterprise within the past twelve years," the authors assert.[10]

Commercial activity by nonprofits is not entirely new; data on revenue sources of nonprofits in the mid-1970s make it clear that even then there was substantial dependence on non-donative revenues--either from membership dues or from some form of sales. As early as 1908, the Metropolitan Museum of Art opened a sales shop; even before that it sold copies of photographs from its collections. College bookstores have long existed to sell course materials. One of the best known examples of sales of goods to generate income for a nonprofit organization is the annual Girl Scouts cookie sale. In 1982 the Girl Scouts of America sold 125 million boxes of cookies for gross revenue of over $200 million.[11]

Some of the new activities that nonprofits are moving into as part of their tax-exempt efforts will come to be questioned as sufficiently remote from the purpose for which tax-exemption was granted that the net income is subject to taxation as "unrelated business income" (UBI). Some of these activities are so clearly unrelated to the organization's exempt purpose that they are organized into separate for-profit entities.[12] In other cases the new activity will be in the "gray" area; this is likely to constitute a growing administrative problem for the IRS, as financially hard-pressed nonprofits increasingly probe the outer limits of exempt-income activities. A 1985 report by the federal General Accounting Office (GAO) points out that this is already a problem. IRS does not have sufficient information on UBI [unrelated business income] tax noncompliance to fully understand the nature and magnitude of UBI noncompliance and develop profiles of high noncompliant tax-exempt organizations engaging in UBI activity.[13] The GAO report notes the limited staff available to the IRS for investigations, the "increasing UBI activity," and the substantial rate of noncompliance that their audit disclosed. Measured in dollars, non-compliance with the tax on unrelated business income was estimated at 25 percent for social welfare organizations, but 58 percent for charitable and educational organizations and 61 percent for business leagues.[14]

When nonprofits seek profitable enterprises they almost inevitably move away from charitable and collective-type services and into the sale of private-type goods. The pursuit of funds thus drives nonprofits into competition with private sector enterprises. Recent research supports the expectation that when the budgets of nonprofit organizations are squeezed, they respond by shifting attention to sales of goods in private markets. Jerald Schiff and I hypothesized that nonprofits pursue the goal of maximizing their output of a "charitable" service, subject to the necessity of at least breaking even financially.[15] We see nonprofit as a potential provider of two kinds of goods or services--charitable and "private"; the organization managers and directors prefer to produce the charitable good, which is financed by private donations and by government support, but they may resort to selling private output to "cross-subsidize" their charitable activities. This model of behavior, to the extent it is correct, implies that the private business sector does, indeed, have something to fear insofar as reductions in government support prompt the nonprofits to extend their activities into markets for private goods.

In this framework, a change in government expenditures can have a number of effects on nonprofits: (1) the direct revenue effect of the change in government spending; (2) a "crowding out" effect; (3) a revenue-source substitution effect (this is the effect giving rise to private firms' fears of nonprofits' competition--as cuts in revenue from government or from private donors cause nonprofits to increase sales of less preferred, private-type outputs); (4) fundraising effects (changes in government spending can affect the optimal level of nonprofits' solicitation expenditures for private donations); and (5) exit/entry effects (government budget cuts can affect the number of nonprofit organizations).

Utilizing data from tax returns of the more than 11,000 social welfare nonprofits in the United States between 1973 and 1976, Schiff and I estimated the effects of changes in various types of government welfare spending--cash transfers, purchases from nonprofits, and direct governmental provision of services--on the variables listed above.

Our study allowed for interactive effects whereby, for example, a cut in government purchases from nonprofits could affect the level of an average nonprofit organization's revenue in a number of ways--directly decreasing it and indirectly either increasing it or diminishing it further as nonprofits then changed their fund-raising (solicitation) expenditures and their efforts to sell private goods for the purpose of cross-subsidization.[16]

Schiff and I found that most of the expected effects in fact occurred. Changes in government welfare expenditures do exert a statistically significant impact on the level and composition of revenues--as between donations and sales--for nonprofit welfare organizations, but the magnitude and even the direction of effect differs depending on whether governments change their cash transfers, direct provision of welfare services, or purchases of services from nonprofits. When governments reduce their direct provision of social services, the nonprofit sector responds by increasing its sales activities. A 10 percent cut in government social service spending would cause nonprofits to increase their sales by an estimated 1.3 percent.

This finding, that reduced government spending, by adversely affecting nonprofits' ability to finance their preferred charitable activities, leads to increased sales efforts, is derived from study of only welfare organizations. The general question, though, of how nonprofits' sales activities respond to changes in the availability of various forms of public and private revenue, remains open; Schiff and I also found, for example, that cuts in other forms of governmental welfare spending--on cash transfers--do not bring adjustments that increase nonprofits' sales revenues.

The question of whether nonprofits should be restricted, taxed, or even prohibited from competing with the proprietary sector is moving increasingly into the policy arena. A growing number of nonprofits see access to profit-making activities as indispensable. But an increasing variety of proprietary firms are challenging the proposition that competition from nonprofits is wise public policy. A recent survey by the Congressional General Accounting Office found, for example, that 84 percent of private research firms and 90 percent of racket-sport firms claim that nonprofit, tax exempt universities and fitness groups compete unfairly with them.[17]

A critic of university-based research sales claimed that "Colleges and universities and independent nonprofit organizations offer [research] services in competition with for-profit firms as a by-product of tax-exempt 'basic' research and education functions. ... faculty entrepreneurs are able to underprice local firms because they do not have to factor equipment and other capital costs into their prices."[18]

Nonprofit hospitals are expanding "vertically" into a growing number of for-profit activities that either provide services to hospitals or that provide services on the recommendation of hospitals. Thus, nonprofit hospitals and clinics are increasingly moving into the retail end of the hearing aid industry.[19] They have also begun marketing laundry services, in direct competition with local private laundry services. And three nonprofit hospitals in the Philadelphia area have begun manufacturing prosthetic devices, in competition with private manufacturers of artificial limbs.[20]

One overall indicator of competition between proprietary and nonprofit organizations in various industries is the importance of sales revenues to the nonprofits. When nonprofits generate revenues through sales, they are probably providing outputs in competition with proprietary firms, whereas when they generate

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donations they are probably providing outputs that differ in type from what the proprietary market provides.[21] Thus, the average nonprofit in the legal aid industry is not very competitive with its proprietary counterparts, for these nonprofits receive only 3 percent of their revenues from "sales." In scientific research, by contrast, the average nonprofit appears to be much more like its proprietary counterparts, for it receives 86 percent of its revenues from sales.

Another overall indicator of competition between proprietary and nonprofit sellers is the relative size of the nonprofit component of mixed industries. The larger the nonprofits' share of sales in an industry, the greater is its impact on the for-profit component. Among blood banks, nonprofit facilities in the mid-1970s were only one-tenth as numerous as proprietaries; in nursing homes there were fewer than one-third as many beds in nonprofits as in proprietary homes. By contrast, in child day care, nonprofits handled 80 percent as many children as proprietaries, among renal dialysis centers nonprofits were nearly 3 times as numerous as proprietaries.

When a nonprofit seeks to sell some outputs profitably in order to fund other activities (that is, to cross-subsidize), it must find outputs that are both saleable and profitable. The position that public policy should take concerning these activities depends on the side effects of permitting or restricting them. Should there be any constraints on the type or level of profit-making activities by nonprofits? One issue is what kinds of money-generating activities are nonprofits likely to engage in, if they were unconstrained? Another is whether it is both economically efficient and equitable that those activities be pursued? Finally, does the tax system deal appropriately with the expansion of nonprofits into the new areas? Currently, this system taxes nonprofits' "unrelated business income" as ordinary corporate profit and for some classes of nonprofits it limits the proportion of total revenue that may be from activities that are unrelated to the organization's exempt purpose.

The policy choices are (a) having a smaller, more "pure" set of nonprofits that are financed by donations, which may leave them less constrained in their activities, and (b) having a larger nonprofit sector that receives more revenue from sales of private-type goods or from those government and private contributions that come with tighter "strings" attached. In my judgment, public policy cannot adopt tax or other measures that drive nonprofits into private-goods markets--that is, toward option (b)-- without compromising nonprofits' principal rationale for existing--their contribution to social welfare.

The cries of unfair competition, by the private sector, result partly from judgments about how to define a nonprofit's unrelated business income. That income is fully taxable; in that sense nonprofits are somewhat discouraged from engaging in the activities that generate it. Under the law, net income for a nonprofit is taxable if it resulted from an activity that is not "substantially" related to the "charitable, educational, or other purpose which fixes the basis for its exemption under Internal Revenue Code Section 501."[22] Depending on how broadly or narrowly the IRS interprets the "exempt purpose" of the organization, the nonprofit will have a larger or a smaller domain into which it can compete with proprietary firms at a competitive tax advantage.

The tax law did not always restrict, tax, or otherwise handicap nonprofits' revenues, as it now does. In 1948, when a group of alumni donated the Mueller Macaroni Company to the New York University (N.Y.U.) Law School, Mueller's profits were given tax-exempt status because N.Y.U. was a nonprofit organization.[23] But two years later, in an apparent attempt to deal with the "unfair competition" issue, Congress amended the Internal Revenue Code to exempt from taxation only the "related" business ventures of nonprofits.[24] Concerns about "unfair" competition by nonprofits somehow became translated into business activity that was not "substantially related" to the exempt purpose.

Administrators and courts have found it very difficult to deal with many specific situations in which they have had to apply the "substantially related" concept. One Circuit Court judge referred to "hair-splitting" decisions in a case involving whether sales by a nonprofit hospital's pharmacy to private non-hospitalized patients of physicians on the hospital staff were tax-exempt.[25] A former Commissioner of the Internal Revenue Service, Sheldon Cohen, expressed the frustrating complexity of distinguishing taxable from non-taxable income of nonprofit organizations: "Nonprofits are a whole can of worms that Congress has yet to look at in a broad way. I have been blowing the trumpet for years to get lawmakers to spell out clearly what should be tax-exempt and what should not be."[26]

The ambiguity of a nonprofit's exempt purpose could be decreased, of course, by a change in the law and its administration. The exempt purpose could be defined more precisely and narrowly. Currently, nonprofits are granted exempt status for such broad purposes as education or community development. How broad should the definition of a nonprofit's exempt purpose be? Proprietary firms would like to see it be narrower, so that nonprofit organizations would be more restricted. Nonprofits would like it to be broader, giving greater flexibility. Weighing such conflicting arguments is very difficult. The perspective of a tax-collection agency--such as the IRS--is not the most appropriate one for doing this balancing.

Another question--seemingly technical, but of considerable import--is how a nonprofit organization's costs should be allocated between its exempt and non-exempt ("unrelated") activities. When it is producing both, it is in a position to exercise discretion in the way it allocates certain costs--such as for capital equipment, office space, and salaries--that apply to both. It has the incentive, of course, to allocate as much of these joint costs as possible to the otherwise-profitable unrelated business activities, so as to minimize reported taxable net income and hence tax payments. Nonprofits that may appear to make little profit on the unrelated business activities, where they compete with proprietary firms, may actually make substantially greater profits. This is an additional source of administrative headache for the IRS; it seems an additional source of unfair competition to proprietary firms.

Through a variety of tax laws and subsidy programs, nonprofits are treated as worthy of explicit encouragement. At the same time there have been actions that effectively reverse such institutional encouragement. A recent decision by the Office of Management and Budget (OMB), for example, resolves, at least for now, one element of the unfair competition debate. It involves competitive bidding between nonprofit and for-profit firms for federal government contracts. Proprietary firms have argued that their bids are higher simply because they must pay federal, state and local taxes that their nonprofit competitors do not. In August 1983, the OMB altered its rules on bidding for federal government contracts. Any Federal government agencies are now required to take into account, in awarding a contract, an estimate of the tax revenue foregone if the contract is awarded to a nonprofit: "If the apparent low bidder or offeror is a tax-exempt organization, the contract price must be adjusted by an amount equal to the Federal, state and local income taxes that would be paid by the lowest non-tax-exempt bidder or offeror. This adjustment is necessary to determine which bidder or offeror has the lower overall cost to the Government."[27] The rules also specify how the federal government is to choose in the case of a tie between a nonprofit, tax-exempt organization and one that is not. If the tax-adjusted price is identical to the non-tax-exempt organization's price, the non-tax-exempt organization is the winner.[28]

There is a paradox. Society seems to have an unarticulated but de facto policy that sees an important difference between the social desirability of nonprofit activities when they are supported by donations (most of which are contributed indirectly, through the tax system, by taxpayers in general) and when they are supported by sales of goods in private competitive markets. If this is the basis, even in part, of the patchwork public policy toward nonprofits, it is important to learn more about the validity of the proposition that the source of revenue affects the nature of output. This is one more example of the weak analytic and factual base that now underlies policy toward nonprofits.

Do Nonprofits Have a Net Advantage?

However the nonprofits use the funds generated from competitive sales, another important factual question is just how great is the alleged advantage that nonprofits have when they compete with proprietary firms? This, after all, is presumably the basis of the "unfair competition" complaint. That complaint rests on more than simply the exemption from profit tax and the deductibility of donations to some nonprofits. Beyond the tax-deductibility of donations for some nonprofits, and the exemption from corporate profit taxation for all, nonprofits have both advantages and disadvantages in any potential competition with proprietary firms. There are numerous legal rules that define what can be done with the resources commanded by nonprofits. Some of these rules are more restrictive than those confronting for-profit firms, others are less so.

On one hand, nonprofits may not pay out any surplus or profit to anyone associated with the organization; they are effectively cut off from the market for equity capital. This non-distribution constraint means that the organization must serve a public interest; according to the IRS, the "...prohibition of inurement, in its simplest terms, means that a private shareholder or individual cannot pocket the organization's funds except as reasonable payment for goods and services."[29] Excessive wages or salary, rental charges, or purchase price of property would be evidence of private inurement, although the cost of determining what is "excessive" serves as a clear obstacle to IRS enforcement.

Charitable nonprofits--those that may accept tax-deductible donations--are also severely limited in their freedom to engage in lobbying or in other political activities involving attempts to support or oppose a particular candidate or to influence legislation. These constraints are comparatively recent. The prohibition on participation in political campaigns originated in a Senate floor amendment added by Lyndon Johnson in 1954. Johnson apparently believed that a foundation in Texas had provided financial support for his opponent in an election.[30] Such a limitation on attempts to influence legislation originated earlier, though, in a 1934 Senate floor amendment; the sponsor indicated irritation with the activities of one specific nonprofit organization, the National Economy League.[31]

The limitation on legislative lobbying--which does not apply to proprietary firms--has posed enforcement problems that attenuate its effectiveness. Internal Revenue Code section 501(c)(3) states that "no substantial part of the activities" of a charitable organization may be used for "carrying on propaganda, or otherwise attempting, to influence legislation." The term, "substantial," is obviously imprecise. It has been interpreted to mean more than 5 percent of an organization's time and effort;[32] under the Tax Reform Act of 1976, however, most charitable organizations (although not churches and some others) have the option of electing to come under specific expenditure limitations rather than the vague "substantial" criterion. Under this option, an organization is permitted to spend on lobbying up to 20 percent of the first $500,000 of its expenditures (exclusive of fund-raising), 15 percent of the next $500,000 and 5 percent beyond that, with a maximum total of $1 million per year. And expenditures aimed at influencing the public on legislative matters are limited to 25 percent of these amounts.[33] Even now, charities are under increasing pressure to restrict lobbying and, indeed, the definition of "lobbying" continues to be a source of contention. As of mid-1987 the IRS is still revising the administrative rules it developed in November 1986, which would, according to 16 members of the Senate Finance Committee, "Severely limit the rights of charities to communicate with legislators and public officials."[34]

The nonprofits, charitable or other, however, are not subject to some constraints that are commonly believed to exist. Most notably, they are not restricted in the amount of profit they may make, only on what they may do with the profits--essentially being constrained to use them to purchase more resources for the organization.

Nonprofits also have a number of tax and subsidy advantages over proprietary firms. Government tax subsidies extend beyond the corporate income tax exemption and, for some, deductibility of donations to them. "Other areas of special treatment or exemption include Social Security,[35] unemployment insurance,[36] the minimum wage,[37] securities regulations,[38] bankruptcy,[39] antitrust,[40] unfair competition,[41] copyright,[42] and postal rates.[43] But even this impressive list is incomplete. On August 27, 1982 a law was signed requiring large firms that are granted patents to pay a user fee equal to 100 percent of the costs incurred by the federal government in awarding the patent; but nonprofit organizations (as well as small firms and independent inventors) need pay only 50 percent.[44] And certain nonprofits--those charitable-type organizations that are tax-exempt under section 501(c)(3) of the Internal Revenue Code--are exempted from the section of the Organized Crime Control Act that prohibits gambling businesses.[45]

Many nonprofit organizations also benefit from favored tax treatment by the individual states in which they operate. Most states exempt them from paying sales taxes on their purchases and from paying property taxes. The property tax exemption has often been the source of considerable hostility between large nonprofit institutions, such as universities, and local government officials who see that they are obliged to provide police, fire and other public services to the nonprofits but receive no property tax payments in return. Sometimes the nonprofits make voluntary payments in lieu of property taxes, but even in those cases the amount of the payment is frequently debated. And the exemption from property taxation may induce nonprofits to utilize more capital-intensive and land-intensive production processes than do proprietary firms, which must pay such taxes.

Considering all these differences between nonprofit and proprietary organizations, what is the net effect on competition between them? In one sense the answer is clear: Nonprofits enter into competition with proprietaries only when they expect to be able to compete effectively and, when if is revenue they are seeking, to do so profitably. They compete with travel agencies, testing laboratories and hearing-aid sales, but not with mining companies, steel mills and department stores.

Only a little is known about the quantitative importance of the various subsidies that are provided to nonprofits. Because these subsidies differ from state to state--even though the federal portion is the same across all states--it is possible to determine whether there is a systematic relationship between the magnitude of a state's subsidy to a nonprofit organization and the size of the nonprofit sector relative to the proprietary sector in that state. This information is vital; it helps answer the question of what effect various public subsidies have on the ability of nonprofit organizations to survive and to compete with proprietary firms.

The higher the level of a state's taxation of private business, the greater the competitive value to a nonprofit of exemption from those taxes. Thus, in states that have higher property tax, sales tax and corporate income tax rates, nonprofit organizations receive, in effect, a greater subsidy than they do in states with lower tax rates. Nonprofits have a larger market share in the higher-tax states.[46] In the competition between nonprofit and proprietary firms, tax exemption of nonprofits makes a difference--particularly the exemption from sales and corporate income taxes. Exemption from property taxation gives nonprofits a particular incentive to locate in central city areas, where property tax rates are usually high.

Granted that tax and other subsidies to nonprofits enhance the ability of nonprofits to compete, is there something "unfair"? Should laws or their administration be changed so as to reverse the inroads of nonprofits into proprietary markets? The two separable issues are competition in the specific industry for which the nonprofit has been given exempt status and competition in industries or activities unrelated to those for which exempt status was given. There is also a considerable gray area between the two.

The first arena of competition might seem to be uncontroversial. Congress has determined that the nonprofit form of organization should be encouraged--that is, subsidized--to engage in certain activities. If those subsidies give the nonprofits a competitive advantage, that is the intent. If proprietary firms are handicapped or even driven from the market, so be it.

However, this model of the legislative process is too simple. It assumes that government has determined that the nonprofit form of institution is socially preferred on either efficiency or equity grounds, but that nonprofits would not exist to an appropriate degree without subsidization. Government is credited with considerable knowledge and a decision process that leads to maximization of "social welfare." But the facts are far from clear. Evidence that nonprofit hospitals are more "public-serving" than are proprietary hospitals, for example, or that nonprofit schools, nursing homes, day care centers, or publishers deserve encouragement relative to their proprietary counterparts is by no means overwhelming. It is fair to say that serious attempts to detect the social rationale for encouraging nonprofits in particular areas of economic activity have been scant and indecisive, at least outside of health care.[47]

The potential advantage the nonprofit form of institution has over proprietary firms for poorly informed consumers implies that neither the nonprofit form nor the proprietary is likely to be preferred by all consumers. Poorly informed consumers may prefer dealing with a nonprofit because the organization's constraint on the distribution of profit reduces its incentive to act opportunistically. For these consumers, the public subsidies to the nonprofits are valuable. Other, better-informed consumers have no such institutional preference, wanting to deal with any organization, regardless of ownership form, that provides the wanted outputs at the lowest price. Since public subsidies to the nonprofit sector may reduce the number of proprietary firms, for these consumers the competitive advantage granted to nonprofits seems counterproductive, inefficient, and unfair.

The second arena for competition is in markets for unrelated outputs--where nonprofit organizations seek to reap profits for use in their "primary," exempt activities. Here the issue of "fairness," as the affected proprietary firms see it, or of economic efficiency, as an analyst with an economic welfare perspective might view it, is cloudy at best. Some parts of an analytic framework for informing public policy on how far nonprofits should be permitted to reach out to complete with proprietary firms involve two sorts of interdependencies: in costs, between a nonprofit's costs of producing its primary outputs and its costs of producing various other, "unrelated" outputs, and in revenues, between a nonprofit's ability to generate revenues from its primary activities and its ability to obtain revenues from various other outputs.

If there were no such interdependencies--that is, if both production costs and revenues for a tax-exempt commodity, X_1, and another, unrelated, commodity that is not tax-exempt, X_2, were independent of each other--a nonprofit producer of X_1 would have no advantage in the market for X_2; it would have to compete with for-profit firms in the latter market, where consumers would patronize the more-efficient suppliers, regardless of ownership type. But the assumption of independence is not likely to hold. Nonprofits that seek new product markets where they can make profit to augment their receipts of donations will select precisely those products and services where their initial, subsidized production of X_1 provides a competitive advantage.

The advantage could involve costs. Consider a proprietary firm engaged in product testing or archaeological work that complains about competition from a nonprofit university because the university can employ graduate students inexpensively since they are already on campus for their education. The firm is arguing, in effect, that graduate students are joint inputs to the production of both their own education and these other research activities. It should come as no surprise that the university would find it efficent and profitable to make use of just such cost-saving opportunities, rather than to engage in any of a myriad of other production activities--such as mining or automobile production--in which the resources utilized in its educational activities would give it no advantage.

Such joint-cost economies, representing real efficiencies, are also the basis of a public policy dilemma. Given that an organization--in this case, a university--is producing tax-exempt outputs, X_1, it can be economically efficient for it also to produce certain other, non-tax-exempt, X_2 outputs. But at the same time, expansion into the latter markets brings the subsidized organization into direct competition with unsubsidized firms in the proprietary sector of the economy. For-profit firms may claim unfair competition; yet that competition is efficient, given the initial judgment that there are type-X_1 commodities that merit subsidization through nonprofit organizations.

Joint costs may seem to be a technical matter that can be handled by accountants and that involves no major policy choices, but such a view is wrong. Yet the choice has important policy implications when the various outputs are subject to differing regulatory and subsidy standards, some being tax-exempt, others not.

The Court, while striking down laws that place limits on fund-raising, has not objected to laws that require nonprofits to provide information about their fund-raising percentage. Yet the problem of how to allocate joint costs remains; there is no "correct" division of truly joint costs. Regulatory agency pressure for release of such information--regulation that implies that a higher proportion of fund-raising is undesirable--will cause nonprofits to search with their accountants for ever more "creative" ways to show that their cost of fund-raising is small. Increased information requirements may lead to re-definition of terms and changes in accounting practices that may provide donors with less information. This could lead to even greater regulatory involvement, with increasingly detailed specification and monitoring of nonprofits' accounting practices.

The same problems arise as nonprofits expand into profit-making activities that generate unrelated business income. By charging much of the joint costs to the for-profit enterprise, the nonprofit can reduce, if not eliminate, its UBI, which is taxable, even though the activity is actually quite profitable. By the same token, private or public contributions for the nonprofit's "main" (exempt) activities permit purchase of resources that can be used jointly in both that and other activities; thus, if nonprofits are permitted to extend their activities, donors' contributions constitute a "joint subsidy" for all of the organization's activities--whether intended or not--including those that are substantially "unrelated" to its exempt purposes.

Nonprofits seeking additional revenues can be attracted to new activities not only because of cost-interdependencies but also because of consumption interdependencies in demand. Thus, consumers who are obtaining X_1 from a nonprofit organization may also prefer to purchase other, X_2, goods and services, from it. Indeed, a nonprofit organization in search of profits will seek out just such relationships. For example, patients leaving a hospital may prefer to buy prescription drugs from a pharmacy at the hospital rather than from another down the block. These examples illustrate the effect of consumer preferences on nonprofit organizations. Prescription drugs are are already available through proprietary firms and so there is no obvious failure of the private market. But at the same time, consumers who visit a hospital or come to a PPA office for counseling doubtless find it convenient to purchase prescriptions. Similar complementarities for consumers seem to be at the root of a number of claims of unfair competition, such as hospitals selling hearing aids and universities providing travel-agency services. If consumers do prefer to purchase a variety of goods and services from the same source, then to restrict a nonprofit's outputs would hurt consumers. Yet to permit the nonprofit to expand its activities would hurt proprietary producers. [48]

A number of proposals are now being considered to reduce competition from nonprofit organizations with proprietary firms. The interdependencies in production costs and in consumer demands make it very complex to evaluate the proposals from an overall societal perspective. One of the current plans to limit nonprofit business activities would increase the tax rate on the first dollar of UBI of the nonprofits, setting it at the highest marginal corporate tax rate, 46 percent, rather than at the lowest, 16 percent. Another would totally prohibit unrelated business activities. Still another would alter the criteria for determining what is an "unrelated trade or business," so that the IRS would consider not only whether an activity is "substantially related" to the organization's exempt purpose, as it does now, but also its impact on proprietary firms. There is also a proposal to amend the Federal Trade Commission (FTC) Act, which exempts nonprofits from the restrictions on unfair competition.[49]

Complaints of unfair competition do not come only from the private sector. Nonprofits, too, claim that "business has entered customarily nonprofit fields as health and child care."[50] There may well be a tendency for each form of organization to argue that incursion of the other form into an activity dominated by the other is "unfair," but surely the appropriate social roles for the private and the nonprofit sectors cannot be determined by which form of organization was "first"--even if that were clear.

Nonprofits do not have access to the market for equity capital, which is a mainstay of for-profit firms. Insofar as nonprofits provide public-type goods they face the problem of free-rider behavior, which restricts suppliers' ability to sell outputs to individual consumers, the ultimate source of revenues for proprietary firms. By contrast, for-profit firms find it costly, if not impossible, to obtain donations, which are enormously important for nonprofit organizations.

Subject to these varied constraints on fund-raising, any organization can affect the amount of money it receives from each source. A proprietary firm can affect its revenue from sales by changing the level and quality of output, as well as its price, assuming it does not operate in a perfectly competitive market. A nonprofit organization can affect the amount of donations it receives, through fund-raising activities; it can also alter the amount of funds available for its primary, tax-exempt purpose by engaging in the production of other goods and services that can be sold at a profit, with the profits being used to finance the primary activities.

When nonprofits move into these "secondary" markets they act more and more like proprietary firms, as they become increasingly competitive with the proprietaries. Proprietary firms now claim, with growing stridency, "unfair" competition from the subsidized nonprofits that are expanding into the traditional markets of private enterprise. This truly poses a dilemma for public policy.

Notes

1. These data are from my random sample of 274 tax-deductible (501 (c) (3)) organizations for the tax years 1973-1975. The distribution of organizations, by the percentage of revenue coming from donations is in Appendix table A6.1.

2. SBA News, Number 83-41.

3. Susan T. Schmidt, "Survival of Nonprofits May Depend on Their Entrepreneurial Savvy," Washington Post, July 27, 1983; and Unfair Competition by Nonprofit Organizations With Small Business: An Issue for the 1980s (Washington, D.C.: U.S. Small Business Administration, June 1984).

4. Jack Norman, "Lean times for largesse," The Milwaukee Journal, October 17, 1982, Business Section, 1.

5. Meg Cox, "At Some Eateries, People Just Eat; At This Cafe, They Also Do Good," Wall Street Journal, September 18, 1985, 25.

6. "Business Ventures for Nonprofits, 1984 Schedule," (Los Angeles: The Grantsmanship Center, 1984), 2.

7. William Fulton, "The Robin Hood of Real Estate," Planning, May 1985, 4-10.

8. Jane Mayer, "Survival Tactics: Cuts in Federal Aid Lead Public TV to Try a Bit of Free Enterprise," The Wall Street Journal, March 10, 1982.

9. James C. Crimmins and Mary Keil (Washington, D.C.: Partners for Livable Places and The Rockefeller Brothers Fund, 1983).

10. Ibid., 14.

11. Edward Skloot, "Enterprise and Commerce in Nonprofit Organizations," in Handbook of Nonprofit Organizations, (New Haven, Ct.: Yale University Press, 1985).

12. For a number of examples of nonprofits that have formed for-profit subsidiaries, and the reasons for their doing so, see Robert Mier and Wim Wiewel, "Business Activities of Not-for-Profit Organizations," American Planning Association Journal, Summer 1983, 316-325.

13. "Where is IRS Likely to Look in 'Unrelated Business Income' Audits?" Philanthropy Monthly 85 (September 1985), 13-16, at 13.

14. Ibid., 13, 15.

15. Jerald Schiff and Burton A. Weisbrod, "Government Social Welfare Spending and the Private Nonprofit Sector: Crowding Out, and More," November 1986.

16. That is, starting with a system of four structural equations positing the factors affecting an average nonprofit's receipts from (1) donations and from (2) sales, its (3) level of fund-raising expenditures, and (4) the total number of welfare nonprofits in a state, Schiff and Weisbrod estimated reduced form equations which reflect the interactive effects. The methodology is described in detail in the paper, Ibid.

17. "Does Charity Trespass on business's territory, or vice versa, or both? Wall Street Journal, March 18, 1987, 1.

18. Statement of Charles Garber, President, Structure Probe, Inc., West Chester, Pennsylvania, before the Symposium on Nonprofits Competition with Small Business, July 27, 1983, as presented in Unfair Competition, 21.

19. Statement of James Lovell, National Hearing Aid Society, before the Symposium on Nonprofits Competition with Small Business, July 27, 1983, as presented in Unfair Competition, 23.

20. Unfair Competition, 24.

21. I say "probably" because it is possible for proprietary firms to receive donations that would be used to do much of what nonprofits do with those revenues. The principal problem, however, is the difficulty donors have in monitoring the outputs and to whom they are distributed.

22. Internal Revenue Code, Section 513.

23. Susan Rose-Ackerman, "Unfair Competition and Corporate Income Taxation," Stanford Law Review, 34 (May 1982), 1017-1039.

24. The legislative history stated explicitly that "The problem at which the tax on unrelated business income is directed is primarily that of unfair competition." S.Rep. No. 2375, 81st Cong., 2d. Sess. 28-29 (1950).

25. Hi-Plains Hospital v. United States, 670 F.2d 528 (5th Cir. 1982).

26. "Special Report: For Many There Are Big Profits in 'Nonprofits,'" U.S. News and World Report, November 6, 1978.

27. *Supplement, OMB Circular No. A-76 (Revised), Performance of Commercial Activities*, Executive Office of the President, Office of Management and Budget, August 1983, IV-35-36.

28. Ibid., IV-36.

29. *IRS Exempt Organizations Handbook*, (IRM 7751) sec.342.1(1), as quoted in Bruce R. Hopkins, *The Law of Tax Exempt Organizations*, 2nd edition (Washington, D.C.: Lerner Law Book Company, 1977), 128.

30. Hopkins, Ibid., 154.

31. Hopkins, Ibid., 143.

32. Hopkins, Ibid., 145.

33. Hopkins, Ibid., 149.

34. Scott R. Schmedel, "Charities Lobby Hard to save their right to lobby," *Wall Street Journal*, March 11, 1987, 1.

35. 42 U.S.C. Section 410(a)(8)(B)(1976).

36. 26 U.S.C. Section 3306(b)(5)(A), (c)(8)(1976).

37. 29 U.S.C. Section 203(r)(1976); 29 C.F.R. Section 779.214(1982).

38. 15 U.S.C. Section 77c(a)(4)(1982).

39. 11 U.S.C. Section 303(a)(1982).

40. See *Marjorie Webster Junior College* v. *Middle States Association of Colleges and Secondary Schools*, 432 F.2d 650 (D.C. Cir. 1970), *cert. denied*, 400 U.S.965(1970).

41. 15 U.S.C. Sections 44,45 (1982).

42. 17 U.S.C. Sections 110, 111(a)(4), 112(b), 118(d)(3)(1976).

43. 39 U.S.C. Section 3626(1976).

44. Letter from U.S. Senator Lowell Weicker, Jr. to the *Wall Street Journal*, September 29, 1982, 33.

45. Bruce R. Hopkins, *The Law of Tax Exempt Organizations*, 2nd edition (Washington, D.C.: Lerner Law Book Co., 1977), 18.

46. Henry Hansmann,"The Effect of Tax Exemption and Other Factors on Competition Between Nonprofit and For-Profit

Enterprise," Program on Nonprofit Organizations, ISPS, Yale University, July 1985.

47. National Academy of Sciences, Health Care For Profit, 1986; and B. Weisbrod and Mark Schlesinger, "Public, Private, Nonprofit Ownership and the Response to Asymmetric Information: The Case of Nursing Homes," in Susan Rose-Ackerman, ed. Economics of Nonprofit Institutions, 133-151.

48. Whether the nonprofit "provides" the service directly or contracts it out is not important. Even in the latter case the nonprofit would presumably benefit virtually as much from the rent it could realize as from the profit it could earn.

49. These and other measures designed to make it more difficult for nonprofits to compete with for-profit firms are discussed in U.S. Small Business Administration, "Unfair Competition by Nonprofit Organizations With Small Business: An Issue for the 1980s," (Washington, D.C., June 1984), 37-41.

50. Scott R. Schmedel, "Does Charity Trespass."

WORKING DRAFT

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THE PROSPECTS FOR VOLUNTEERING OVER THE NEXT FIVE YEARS

by

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Prepared for the 1988 Spring Research Forum
"Looking Forward to the Year 2000:
Public Policy and Philanthropy"

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INTRODUCTION

At first glance, it may seem inappropriate to think of volunteers as an aspect of financing nonprofit organizations. Clearly, nonprofit organizations are highly dependent on attracting, utilizing and motivating volunteers to accomplish their goals, but are volunteers really a financial resource?

There are three ways in which volunteers are clearly an important financial resource. First, the value of their donated time. Independent Sector used 1985 survey data to estimate the monetary value of the time donated by volunteers in the course of a year. Even looking only at the time donated to charitable organizations, the financial resources donated amounted to $84 billion. 1/

Second, data from a more recent national survey conducted for United Way and other nonprofits indicate that 52% of volunteers reported being involved in fund-raising activities. 2/ In that sense, volunteers are a large part of the fund-raising process that allows charitable organizations to meet their financial goals.

Third, virtually every study examining the subject finds that those who volunteer to any charitable cause are more likely to be donate money to charity. 3/ Whether giving precedes volunteering, or the other way around, doesn't matter very much. It is enough to say that involvement breeds further involvement, with positive impacts on fund-raising.

The importance of volunteers, and in expanding their numbers, is recognized by United Way of America and Independent Sector, both of which have ambitious programs and goals for doubling the number of volunteers in the next five years.

The purpose of this paper is to examine the prospects for volunteering over the next five to twelve years. To do so, we will look at the current number of volunteers to charitable organizations, the variables which tend to influence volunteering, and the ways in which charitable organizations may be able to increase the number of volunteers. Finally, we will look at some of the implications for charitable organizations of being attentive to the wants and needs of volunteers, with the assumption that such attentiveness will be vital if we are to dramatically increase and retain volunteers.

VOLUNTEERING: ESTIMATING THE NUMBER OF VOLUNTEERS

For estimating the number of volunteers, we rely on a recent study carried out for United Way of America and other charitable organizations by the Gallup Organization. 4/ This multi-sponsored study used personal, in-home interviews with a nationally representative sample of 1,033 adults, 18 years of age and older. In addition to the multi-sponsored questionnaire, United Way purchased additional proprietary questions. The interviews were conducted in September 1987.

Respondents were asked if they had volunteered to a "religious, charitable, not-for-profit or fund-raising organization" in the past 12 months. When the question is put in this way, 16% of the population report that they have volunteered in the past 12 months. Projected against the number of Americans 18 years of age and over, about 176,269,000 in 1985, this comes to 28.2 million volunteers.

This estimate is noticeably lower than that reported by Independent Sector in 1985, probably because of sample and question wording differences. The 1985 study included in its sample 14 to 17 year olds, and included informal volunteering in its definition of volunteering. The 1985 study also included volunteering for for-profit and governmental organizations (21% of volunteers in the 1985 study). The more recent Gallup multi-sponsor study excludes these volunteers with its more stringent question wording, and this, along with the exclusion of informal volunteering, probably accounts for the differences in the estimates.

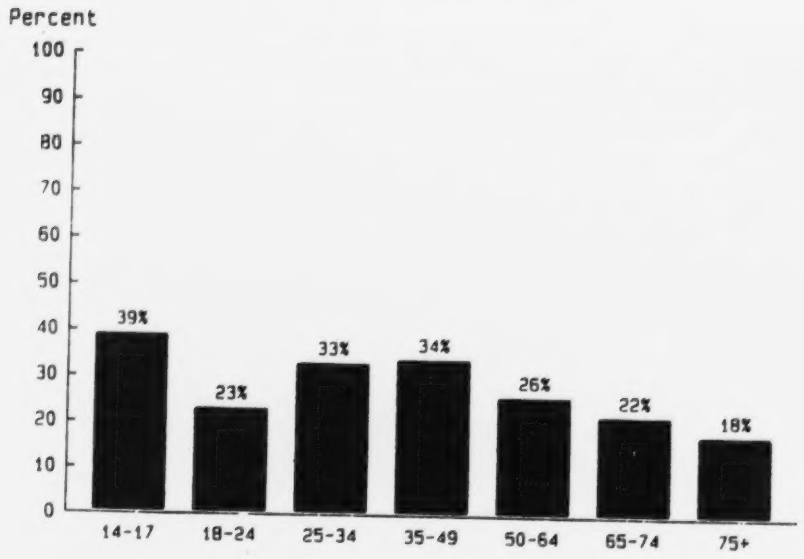
Presumably, when we talk about increasing the number of volunteers, it is those 28.2 million volunteers associated with charitable or nonprofit organizations with whom we are most interested.

DEMOGRAPHIC VARIABLES INFLUENCING VOLUNTEERING

Both the Independent Sector 1985 study and the Gallup 1987 multi-sponsored study show some consistent relationships between certain demographic variables and what can be called "organized volunteering." (That is, excluding those who volunteer informally or alone without a tie to an organization).

Volunteering is related to age in a somewhat curvilinear fashion; the proportion volunteering is highest among those in the 25-34 and 35-49 age groups, but is somewhat lower among those over 50 and those 18-24. The 25-49 age bracket is of particular interest as it includes most of the baby boom generation born between 1946 and 1964, a very sizable demographic group. Figure 1 is taken from the Independent Sector 1985 data, but the 1987 study is consistent with the pattern shown.

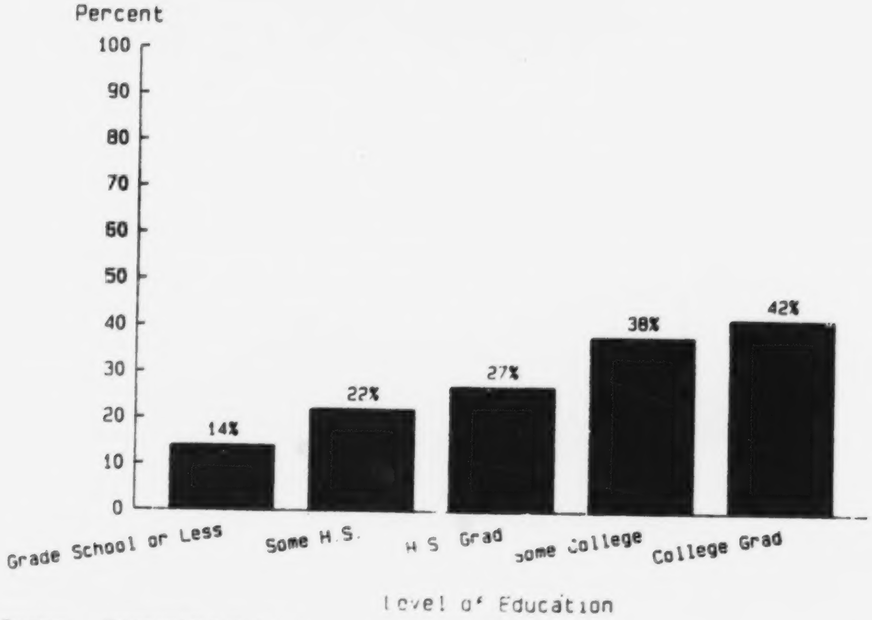
ORGANIZED VOLUNTEERING BY AGE
1985 GALLUP SURVEY



Source: Independent Sector

Education has a strong consistent effect; as education increases, so does formal volunteering in both the 1985 and 1987 studies. As one would expect, income is also related to volunteering, but not as consistently as is education.

ORGANIZED VOLUNTEERING BY EDUCATION
1985 GALLUP SURVEY



Source: Independent Sector

People who are married are more likely to volunteer than those who do not; and the presence of children increases the chances that one will volunteer.

Fifteen percent of males and 18% of females report volunteering in 1987; the Gallup 1985 data showed a similar 3% difference for formal volunteering. Sex is not a significant variable influencing whether one volunteers.

Overall, the picture that emerges from this review of the demographics of volunteering is that the volunteer tends to be a person of above average income and education, who is middle-aged or slightly younger, and domestically settled with a spouse and child.

One way to evaluate the prospects for increasing the number of volunteers over the next 5 to 12 years, then, is to examine Census projections for the key demographic groups and to see whether the number of people in these prime demographic categories is likely to increase or decrease.

PROJECTIONS FOR KEY DEMOGRAPHIC GROUPS

Looking at projections for the key age groups for volunteering, which appear to be those 25-34 and those 35-44 years of age, what are the prospects that these key age groups will grow over the next 5 to 12 years?

Projections of Key Age Groups, 1990 to 2000 (in thousands)

Age	1985	1990	1995	2000
25-34	42227	43529	40520	36415
% change		3%	-7%	-10%
35-44	31839	37847	41997	43743
% change		19%	11%	4%
25-44	74066	81376	82517	80158
% change		10%	1%	-3%

Source: U. S. Bureau of the Census, Statistical Abstract of the United States: 1987

As the table shows, the younger age group will actually increase only slightly between now and 1990, and thereafter decline, according to the middle projection of the Census Bureau. The 35-44 year old group will swell substantially in numbers over the next five years, continue to show impressive growth through 1995, and then decline in numbers between 1995 and 2000.

When both age groups are taken together, the prospects are for a growth of the prime volunteer market of about 10% to 1990; with growth leveling out through 1995, and turning negative between 1995 and 2000.

Income projections indicate that the proportion of households with relatively affluent incomes ($40,000 and over) will increase from 16% in 1980 to 24% in 1995; this would augur well for the next five years. 5/ The proportion of people married, an important variable influencing volunteering, has been stable over the past 4 or 5 years and will probably continue to remain stable. 6/ The proportion of women in the labor force is projected to increase from about 71% (for those ages 25 to 54) to 81% by the year 2000, a much slower rate of increase than in previous years. 7/ To the extent that women entering the labor force shrunk the pool of available volunteers, that impact has already been felt and absorbed.

In sum, it appears that the other demographic variables will not materially alter the pattern we see with the age groups. While the demographic tide is moving the right way in the first five years out, a 10% increase in volunteers is not enough to meet the goals of doubling. Clearly, strenuous efforts will have to be made to recruit and retain volunteers more vigorously if the goal is to increase more than 10% over the next five years; riding the demographic tides with business as usual will not be enough.

RECRUITMENT OF VOLUNTEERS

While nonprofit organizations have little control over the demographic changes in the population, they can do something about their recruitment of volunteers. In most instances, people volunteer because they are asked. It seems logical, then, to focus on the proportion of people that are actually asked to volunteer each year.

According to the Gallup 1987 multi-sponsored study of awareness and involvement, 21% of the public indicate that they have been asked to volunteer to a religious or charitable organization in the past 12 months. Seventy-four percent indicate that they had not been asked. Obviously, one clear path to increasing the number of volunteers is to increase the proportion asked.

There are some indications that this would be successful; according to the Independent Sector 1985 study, 78% of those asked to volunteer accepted, and only 20% declined. Even if allowances are made for overreporting among those who wish to appear altruistic, this is a very good acceptance rate.

What kinds of people are asked to volunteer? To a considerable extent, they resemble the profile drawn earlier of the volunteer. The proportion asked is highest among those between 35 and 49 years of age, among those with college education, and among those with higher incomes. Married people are more likely to be asked than those who are single. Even among these groups, the proportion asked is no higher than 31%, so there is ample room for improvement in these key segments.

The resemblance of those asked to those actually serving raises the question of whether nonprofit organizations need to think about "democratizing the ask." That is, given the large proportion who are not asked to volunteer, there is certainly room to extend the opportunity to volunteer among those with more modest incomes, educational attainments, and those who are older or younger than the typical volunteer.

MODES OF RECRUITMENT

How are volunteers actually recruited? The recruitment process seems to be embedded in the existing organizational and social affiliations people have. If we ask people, as did the Gallup 1987 study, how they were asked, the most frequent response is "by someone in an organization" to which they already belonged (59%). The next most frequent response was being asked by a friend or neighbor (22%), following by being asked at the workplace (14%). Interestingly, mass media approaches (including TV, radio, and print) are cited by only 4% of the volunteers as the way in which they were asked to volunteer.

There are some differences by demographics in how volunteers are recruited. For example, men are 10% more likely than women to have been recruited through an organization to which they already belong, and are about 10% more likely to have been asked at work. Those in the prime age group for volunteering (35-49) are more likely to have been asked by a friend or neighbor than are those who are younger or older.

Given that mass media approaches do not seem to be an effective means for recruiting volunteers, any gains to be realized will have to come through a more effective means of mobilizing people through the organizations in which they belong or through their workplace. A third possibility is asking nonprofit service users and their families.

SERVICE USAGE AND VOLUNTEERING

In a separate analysis of United Way of America's workplace survey database, one of the variables most strongly related to volunteering is whether the respondent or a family member has used the services of a nonprofit or charitable organization in the past 12 months. 8/ Those individuals in the workplace who have volunteered to any charitable organization are much more likely to have been service users (23%) than are non-volunteers, (9%). This suggests that one very effective way of recruiting volunteers, and perhaps of democratizing the ask, is to routinely ask clients or family members of clients to volunteer. We may not always see the service client who as an able volunteer who is willing to help others.

These analyses suggest a four-fold strategy: 1) recruitment and membership drives to expand the total number of people who are members in some standing with a voluntary or nonprofit organization; 2) working through existing organizations to better mobilize their members and to better provide them with opportunities to volunteer; 3) providing opportunities in the workplace to volunteer; and 4) providing service recipients and their families with the opportunity to volunteer.

VOLUNTEER SATISFACTION

An issue often neglected is the danger that a dramatic increase in volunteers could overwhelm many nonprofit organizations' ability to absorb and effectively use new volunteers. New volunteers mean additional training, supervision and matching of abilities, interests, and talents to the needs of the organizations. If many new volunteers are recruited, but are not put to good use, these new volunteers could be negatively influenced by their experience. This could carry over to their attitudes and perceptions of the nonprofit sector generally.

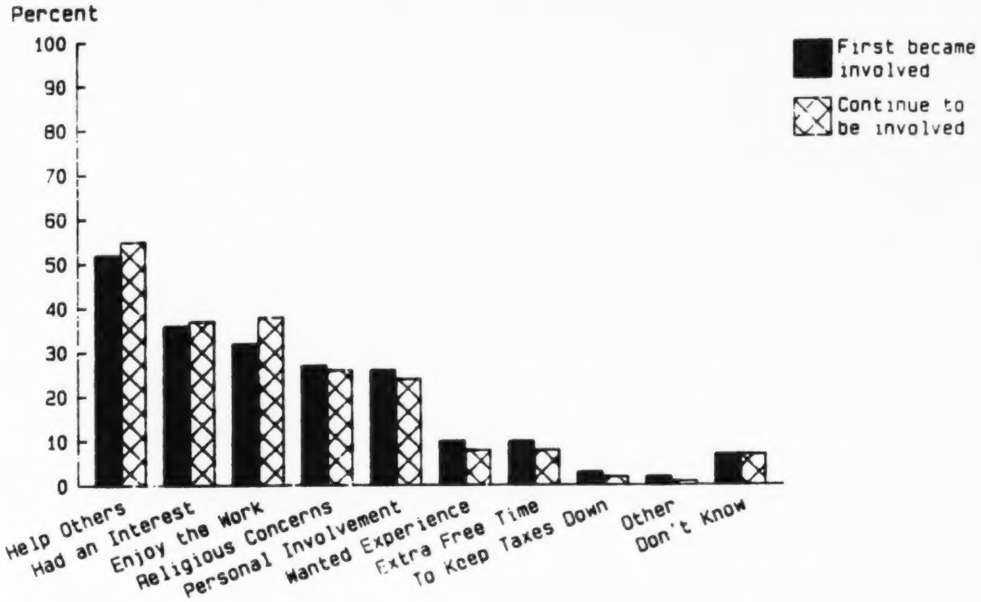
Once we have attracted volunteers, then, how do we increase the chances that the volunteer is satisfied with his or her experience? Related to this, how do we keep the volunteer involved in volunteer activity? The answers to these questions require that we look at the volunteer as a customer, and be attentive to the volunteer's needs and wants.

What are the needs and wants of the volunteer, and what are the implications for how we absorb and handle volunteers?

WANTS AND NEEDS OF VOLUNTEERS

One of the best sources of national data on the wants and needs of volunteers is the Independent Sector 1985 study. 9/ In that study, respondents were asked to indicate the reasons they had for first becoming involved in volunteer activity. The most frequently chosen reason has to do unequivocally with altruism: "Do something useful to help others." However, the second reason, "Had an interest in the work or activity" may combine altruism with an interest in the activity itself. The third most frequently chosen reason has to do with "enjoy doing the work." It very much appears that volunteers become involved partly because they have altruistic needs, but a contributing motivator is the intrinsic worth of the volunteer job.

REASONS INVOLVED IN VOLUNTEER ACTIVITY
1985 GALLUP SURVEY



Source: Independent Sector

This hypothesis gains further support if we look at the reasons people give for continuing to be involved with volunteer activity. While the altruistic motivation remains the most frequently chosen and even increases in importance, the motivation having to do with "enjoy the work" also gains importance.

While the evidence is indirect, it appears that a drive to attract new volunteers needs to address the very real need to help others, but at the same time must offer work for the volunteer that is enjoyable and interesting. In other words, the volunteer job itself must have intrinsic value to the volunteer, as well as altruistic value.

Adding to the challenge is evidence of another need of the volunteer or prospective volunteer. Respondents to the Gallup 1985 survey were asked if they had been asked to volunteer and refused. If they refused, they were asked to indicate why they had refused the opportunity. The predominant reason, overshadowing all others, was "lack of time/too busy."

Lack of time can be seen as an excuse or rationalization, and it probably is for many respondents. However, there undoubtedly remains a substantial proportion of people for whom time is in fact the scarcest resource they manage. Time may be particularly scarce for the growing number of households with children in which both parents work. 10/ This suggests that if charitable organizations were to reduce the amount of volunteer time they expect from each volunteer, they might be able to attract more volunteers.

Of course, this sets up a classic trade-off situation for the charitable organization: can it restructure the volunteer jobs it has to require less time, without neglecting the other needs for interesting and enjoyable work? Can interesting and enjoyable work be provided, without training the volunteer. Once a volunteer is trained, can the organization recover its investment from training the volunteer without demanding a more extensive time commitment?

It is hard to see how charitable organizations can make the appropriate trade-offs without some basic attention to wants and needs of the kinds of volunteers they would like to attract. Some of the information could be gathered through initial questionnaires provided to incoming volunteers; another approach would be to examine the satisfaction of volunteers with their experiences after they have completed their volunteer responsibilities. This second approach is that taken by United Way of America in its pilot work with United Way of Greater Richmond, Richmond, Virginia.

SURVEY OF UNITED WAY VOLUNTEER SATISFACTION

With the cooperation of United Way of Richmond, a list was obtained of 384 volunteers. These volunteers were drawn from a wide range of activities, including planning and allocations committee work as well as fund-raising activity. A questionnaire was mailed to the volunteers; it included items on how the volunteers felt about their experience, their training, and items which measured how satisfied they were with their experience. The response rate was a very respectable 46%.

From this pilot study of Richmond United Way volunteers, we find a very high level of satisfaction from the respondents to the survey. For example, 57% were very satisfied with their volunteer experience, and 92% said that they would volunteer to United Way again. For the most part, data analysis was limited to analyzing the variables associated with respondents feeling very, as opposed to feeling merely somewhat satisfied.

Several key variables in this pilot study of volunteer satisfaction are associated with higher levels of volunteer satisfaction. If volunteers felt that the time demanded of them was "just about right", or "too little", they were more likely to be very satisfied with their experience; those who felt too much time was demanded were less satisfied. If the volunteer felt that he or she had received "hands-on training" they were more likely to be very satisfied. Finally, an awards banquet and an awards presentation by way of recognizing the volunteer's contribution was related to higher levels of satisfaction. However, there was some ambivalence among a substantial proportion of volunteers about how they felt about recognition programs. There may be a need to tailor recognition programs to take account of these feelings.

One reason for involvement was consistently related to satisfaction; those respondents who indicated that a reason for involvement was "enjoy the work" were more likely to be highly satisfied with the experience than those who did not choose that reason.

These results from United Way volunteers in Richmond further underline the need to establish the appropriate dose of time for volunteers, to provide realistic training (rather than just an orientation to the organization), and to offer recognition tailored to the volunteers' views of appropriate recognition. Finally, volunteer satisfaction is enhanced by having volunteers do work they enjoy.

Combined with the indirect evidence from the Gallup 1985 data, it appears that if charitable organizations are able to attract a significantly higher number of volunteers, considerable attention will have to be paid to the issues of how to structure volunteer tasks and training. This in turn may well require volunteer-intensive organizations to invest more heavily than ever before in staff and other resources required to train, supervise, and support them in their volunteer responsibilities.

CONCLUSIONS: THE PROSPECTS FOR VOLUNTEERING

We have shown that the demographic trends over the next five years favor a modest expansion in the pool of likely volunteers. Thereafter, the tides begin to run against increasing volunteers.

We have shown that volunteering is important to charitable organizations, not only for the wide range of activities they perform and the monetary value of the time they donate, but because volunteers, are "cheerful givers." It is vital to the health of the nonprofit organizations that voluntarism continue to grow.

We have also shown that one worthwhile way to increase the number of volunteer recruits is to do a better job of getting the ask out to potential volunteers. When only 21% of the public nationwide is asked to volunteer in a given year, there is obviously ample room for improvement. Increasing the number of people asked, in the short run, can best be done through existing organizations, the workplace and service contacts. It appears that the mass media play a minimal role in this process.

Further, we have shown that there is ample room for widening the base of those who are asked to volunteer. It appears that those asked have a distinctly upscale profile, as do those who actually volunteer. One way to increase the number of volunteers is to "democratize the ask" and provide more people at middle and lower socio-economic levels with the opportunity to volunteer.

Finally, we noted that attention to the wants and needs of volunteers is crucial; charitable organizations cannot risk alienating those who contribute their time by not using volunteers' time effectively. At the same time, these wants and needs can put the charitable organization in a difficult trade-off situation if it wishes to maximize the number of volunteers, improve or maintain the quality of the job itself, and be responsive to the needs of some volunteers to make less of a time commitment initially.

Since so few people are asked each year, and so few actually decline when asked, it appears that the prospects for substantial growth in volunteers are excellent, particularly over the next five years. This success will generate another challenge: making the volunteer experience a satisfying one.

NOTES

1/ Independent Sector, 1987.

2/ The Gallup Organization, 1987.

3/ O'Connor, 1985; Yankelovich, Skelly and White, 1986; Morgan, Dye, and Hybels, 1977.

4/ The Gallup Organization, 1987.

5/ American Demographics, 1984.

6/ Bureau of the Census, 1986.

7/ Monthly Labor Review, 1987.

8/ O'Connor, 1985.

9/ Independent Sector, 1985.

10/ United Way of America, 1987.

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SECTION NINE

REGIONAL AND COMMUNITY ISSUES

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THE MEANING OF PRIVATIZATION FOR NONPROFIT ORGANIZATIONS: THE CASE OF COMMUNITY SERVICES

by

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Prepared for the 1988 Spring Research Forum
"Looking Forward to the Year 2000:
Public Policy and Philanthropy"

San Francisco, California
March 17-18, 1988

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Privatization is the process of shifting production of goods or services from a public administrative arrangement toward a private, market-influenced arrangement. It may be viewed as a conscious strategy for managing public services, or as a movement that has effects beyond those intended to limit expense and increase efficiency.[1] As a strategy it has its adherents[2] as well as its detractors[3]. Those who favor it argue for the greater effectiveness of private organizations to provide public goods. Those who disfavor privatization see the movement as removing collective controls from public, democratic bodies and enabling private parties to benefit through government contracts.

As a movement privatization is a broader, more complex topic to study. Viewed in this way, we would be guided to examine not only public services relocated in (or toward) the marketplace, but also the entry of profit-seeking firms into traditional public-goods industries. Additionally, we would study the alternative strategies available to nonprofit organizations that once relied solely on government funding. From this perspective, privatization might call into question the missions, strategies, and cultures of public-goods organizations. This paper examines these broader effects of privatization on the missions of nonprofit organizations.

Nonprofit organizations (NPO's), because of their legal status and traditional service orientation, are often the organization of choice for privatized government contracts, in such areas as mental health, corrections, child care, and chemical dependency treatment. The growth of the services sector of the economy has brought human service organizations into the foreground of public attention. This, combined with a reduction in directly-operated government programs, the increase in demand for the social services provided by NPOs, and the failure of voluntary dollars to keep up with NPO needs[4] has had the overall effect of creating a competitive environment for many human service NPO's.

The Debate About Privatization

The term "privatization" has been used in three contexts and refers to three somewhat distinct processes. Its most general use refers to the establishment of market economies by emerging nations who are faced with a choice of planning an economy or allowing market forces to distribute goods and services. A second sense in which the term has been used refers to the European practice of selling state-owned, capital-producing industries to private parties. The type of privatization of relevance in this paper is the practice of passing into private hands the responsibility for the provision of public services.

Advocates of privatization argue that public enterprise is inherently less efficient because voters represented by politicians have a smaller stake in efficient production than private owners and therefore monitor public production less closely. Additionally, public office holders are seen as self-interested budget-maximizers who allow inefficiency to flourish[5].

The literature on this type of privatization in social services is growing but there are no good overviews as yet. De Hoog[6] and Schlesinger[7] have both noted that privatization has moved ahead based upon sometimes false or unproven beliefs rather than upon evidence of its efficiency. More critically, Spitzer and Scull[8] associate privatization of police forces with class advantages. Hoch[9] makes a similar argument in discussing municipal incorporation. These arguments link privatization analytically with conflicts between economic classes and control of the state apparatus.

In the most controlled study to date, Stevens[10] compared the costs and quality of eight local government services in twenty southern California cities. No differences were found in quality, but municipal service delivery was found to be 37 percent to 96 percent more costly than the private alternative[11]. All privatized services studied, however, were provided by for-profit organizations. Second, the study did not address "the important political and institutional factors involved in implementing a change from municipal to contract service delivery".[12] Thus, there is no direct evidence of the effect of privatization on NPOs.

The Potential Effects of Privatization on NPOs

The intended impact of privatization is to introduce market forces in the place of administrative arrangements. In the case of NPOs, resource flows have traditionally followed nonrational and informal lines. Certain NPOs have had time-honored relations with United Way, City Hall, or particular local and state government offices. Pressures to make these relations more formal, to open them to competitive bidding, and to institute performance measures arise from both the fiscal pressures felt by funders (private and public) as well as from private interests willing to attempt to profit from some participation. These pressures, however, are unevenly distributed across the community, primarily because not all the services NPOs provide have stable markets. The effects of privatization, then, stem from the nature of competition, the nature of the regulations, and the definition of the market place.

In a market rich in resources, we may expect NPOs to grow in size, as would any rational, profit seeking firm. In a market that appears unstable or shifting, we would expect to see NPOs diversifying their products or holdings, as would any rational, profit seeking firm. Perhaps ironically, the source of resources may not be crucial in determining the effects of privatization on NPOs. Whether the funding is available as fees-for-services or purchase-of-service-contracts or unrestricted grants, competition for these resources should drive NPOs to behave similarly to profit seeking firms.

The central concern for nonprofits is the impact of these conditions upon the integrity of their missions. As the overall volume of resources grows, as regulations change, and as competition increases, traditional missions may be called into question.

Research Questions

With these issues in mind, the broader effects of privatization are tackled here by asking the following questions:

- What is the funding mix (number and proportions) that supports any particular NPO?
- What is the stability of these sources?
- What is the character of relations these different funders? Is performance carefully monitored or is administration otherwise costly?
- Must the NPO compete with other NPOs or PMOs for these funds or their prerequisites (staff or facilities)?
- Are funding shifts related to mission adaptation, clarification, diffusion, or other alteration?

In the interest of brevity, this paper focuses on the influence of funding mixes and shifts on organizational missions. The null hypothesis may be stated as follows:

H_0: Shifting and complex funding mixes will have no impact upon human service NPO missions.

Methods

This study employs a saturation sample of 135 human service NPOs in Louisville, Kentucky. The sample included all nonprofits listed in the local United Way "Directory of Human Services" which listed both United Way affiliates and non-affiliates. A questionnaire entitled "Competition and Personnel Practices in Louisville Nonprofit Agencies" was mailed to 135 NPO executives in October, 1986. The questionnaire included items pertaining to the funding environment, local competition, management practices, and volunteer board recruitment and management. A 77.0 percent response rate was obtained (104 usable questionnaires were returned). Based on responses to the survey, followup interviews were conducted with twelve executives in December 1987.[13]

NPO Funding

A common theme discovered in this study is the wide variety of funders upon which NPOs rely. As shown in Table 1, the average contribution from any particular source of support never exceeded 30.0 percent. This would suggest that human service NPOs attend a fairly complex resource environment.

As one might expect, governmental sources were cited least often by this sample of NPOs. Product sales were the most frequently mentioned source of funds. Nearly half (47.1 percent, or 49 of 104) rely on fees for services, and over half also conducted some regular fund-raising drive. When asked what percentage each revenue source represented in their total annual budget, fees for services led with an average 29.9 percent, closely followed by fund raising (29.6 percent). The reliance on fees for services and the slight role played by product sales echoes the concerns of DeVita and Salamon.[14]

Table 1

Funding Sources in FY 1987 for 104 Human Service Nonprofit Organizations: Selected Statistics*

Source	NPOs Reporting Source		Range	Mean	Median
	percent	(n)		percent	percent
United Way	43.3	(45)	1.0--97.0	22.9	17.0
County	29.8	(31)	1.0--50.0	12.3	9.0
State	32.6	(34)	1.0--70.0	25.7	18.5
Federal	35.5	(37)	1.0--100.0	26.9	20.0
Fees for Services	47.1	(49)	1.0--95.0	29.9	18.0
Product Sales**	15.3	(26)	1.0--100.0	15.3	5.0
Fund Raising	54.8	(57)	1.0--100.0	29.6	24.0

* The table reports percent and number of nonprofits reporting revenues from each source, and the range, mean and median percents from each source for 104 nonprofit human service organizations in Louisville, Kentucky.

** Does not include Girl Scouts or Red Cross.

Table 2 provides a glimpse of whether reliance on fees or fund drives is becoming more or less important to these NPOs. I have reported elsewhere that the majority of NPOs surveyed reported an increase in competition for funds, service areas, and staff with other nonprofit and for-profit organizations in the year preceeding fiscal 1987[15]. Despite increased competition, however, most of those reporting (53.8 percent) reported higher revenues (see Table 2).

The sources of increased revenues, however, bear out the aggregate data reported by DeVita and Salamon[16]. When asked about particular sources, the most frequently cited decrease was in County funds, followed by Federal funds[17]. For those reporting United Way funding, a majority (61.8 percent) reported increases. Fund drives were the most frequently cited as having been sources of increased revenues, at 51.3 percent of those reporting the source, followed by fees for services from private payers (50.0 percent).

Overall it would appear that these organizations are becoming independent of single sources of revenues. This funding environment appears to be shifting, complex, and moving in the direction of non-governmental sources.[18]

Table 2

Funding Changes in FY 1987 for 104 Human Service Nonprofit Organizations: Selected Sources*

Source	lower or decreased		constant or equal		increased or higher	
	percent	(n)	percent	(n)	percent	(n)
Total income	25.8	(24)	20.4	(19)	53.8	(50)
United Way	19.1	(9)	19.1	(9)	61.8	(29)
County	50.0	(22)	29.5	(13)	20.4	(9)
State	25.0	(9	27.8	(10)	47.2	(17)
Federal	38.3	(18)	38.3	(18)	23.4	(11)
Public FFS	22.6	(7)	35.5	(11)	42.0	(13)
Private FFS	14.0	(7)	36.0	(18)	50.0	(25)
Fund Drive	15.5	(11)	25.4	(18)	58.1	(42)
Product Sales	21.5	(6)	50.0	(14)	28.5	(8)

*Rows in this table add to 100 percent; missing cases, and cases not relying on a particular source are not included in the calculations.

In such a complex funding environment it can be difficult to trace the effects of funding shifts on organizational missions. A crude measure is reported in Table 3 which shows respondents' reports of publicly-supported program revenue changes and corresponding changes in services. The table strongly suggests that NPO's are staying with their missions despite declines in government funds. Where public revenues were decreased in 38.3 percent of the fifty agencies operating such a program, services were decreased in only 12.8 percent. Similarly, where public revenues were were increased for 27.7 percent of the agencies, services were increased by 53.2 percent of the agencies. It seems reasonably safe to assert that these NPOs are supporting services with the revenues obtained in fund-raising drives and fees charged to clients. Finally, note once again that product sales do not figure prominently among revenue sources (only 28 NPOs listed the source) and that it was not often among growing sources of revenues).

Table 3

Revenue and Service Changes in Publicly Funded Programs Operated By Nonprofit Organizations*

Item	lower or decreased percent	(n)	constant or equal percent	(n)	increased or higher percent	(n)
Revenue	38.3	(18)	34.0	(16)	27.7	(13)
Service	12.8	(6)	34.0	(16)	53.2	(25)

*Measured by asking executives: "We want to know how funding has changed for programs supported by government. For the most highly funded program your organization operates, has government funding decreased, stayed about the same, or increased over the last five years," and "For the the same program, has your organization provided reduced services, similar services, or increased services over the last five years?"

Personal Interviews

The survey data were amplified by the accounts given by NPO executives in personal interviews. Competition was mentioned frequently but as often in a political context as in an economic sense. One NPO executive director spoke of competition for public money this way:

> First we compete to decide who shall provide a service. Later we compete with other services to determine how much funding we'll receive.

Regarding the problem of competition between worthy services, another executive characterized the whole idea of staying close to government as risky business.

> This organization is facing a choice between being wed to government, increasingly serving indigent populations, having little control over our destiny, and generally living in an unstable environment.

This executive, along with others, complained that government dollars were influenced by political fads. "Last year it was suicidal teenagers, this year it's bored housewives." Another complained that recognizable problems were not always fashionable. Home care for the elderly was economical, for example, but not funded.

The answer that several executives voiced was to subsidize publicly (poorly) supported services with services that could be sold on a fee-for-service basis. Thus, home care could be supported by home health care, which is reimbursable, and chemical dependency treatment for indigents could be supported by the same service sold to insured persons.

This is the juncture at which the question of mission arises. One organization struggled with the decision of whether to open facilities in a relatively affluent part of town.

> We had to look at our history to learn whether we had always served the disadvantaged clientele we see today. We found that our clients are becoming poorer.

The clearest case of diversification occurred in the case of a religious-based organization which works in area of corrections. The organization now operates facilities in three states. The executive of this organization asserted that the values and mission of his organization were its strength, but that "the federal contracts for rehabilitation of criminal offenders increasingly emphasized housing and confinement." Though this executive welcomed the accountability that attended newer contracts, he lamented the competition from larger PMOs:

> I know my competitors. I know their accounting procedures and their business practices...they [the larger PMOs] endanger the quality of services...and our tax advantage is not so great that we can compete.

Like other executives, he was convinced of the value of a mission-oriented nonprofit sector.

Yet NPOs that choose to provide services to paying customers, whether in child care, family counseling, or chemical dependency face competition from PMOs. One executive asserted that

> ...for hospitals, CD [chemical dependency] is an easy loss-leader. The real money for them is in their surgical beds, which they hope to fill once the clients are in the door.

Even where capital requirements are less modest, as in day care, PMOs have considerable market clout. The PMOs have the capital to "cream" the market of its most favorable clients and least costly services. The most threatening development for mental health NPOs is the managed health care system that requires its clients to use in-house services. From the point of view of the NPO, this limits consumer choices.

Conclusion

Ultimately, of course, the issue of service quality and mission must be raised in a discussion of NPOs and privatization. I have taken the position here that the range of possible effects must be considered prior to addressing the issue of quality. There is not a theoretically compelling reason that privatization should have the necessary effect of altering or eroding the quality of services provided by NPOs. However, ultimately, the participation of PMOs in human services could have the effect of leaving nonprofits with the task of providing the most need services with the least resources.

The traditional role of the nonprofit organization in the United States has not been only to supply needed human services but to make those services that are needed known to the public. In the past they have functioned to search out social problems. In a relatively rich resource environment--that is, one which yields returns to aggressive business managers--organizations may flourish while this search function declines. The critical question then becomes, what organizations are recognizing and calling attention to needs, when traditional organizations are busy surviving in established institutional channels?

Notes

1 The President's Commission on Privatization ("Interim Recommendations," December 24, 1987) treats the subject as a strategy for reduction of public expenses in housing, public debt management, air traffic control, education, general contracting out, military commissaries, prisons, urban mass transit, health care, international development programs, postal service, and asset sales.

2 E. S. Savas, Privatizing the Public Sector: How to Shrink Government (Chatham, New Jersey: Chatham House, 1982).

3 Stephen Spitzer and Andrew Scull, "Privatization and Capitalist Development:The Case of Private Police," Social Problems 25 (1977):18-29.

4 Lester Salamon, "Partners in Public Service, the Scope and Theory of Government-Nonprofit Relations," in The Nonprofit Sector: A Research Handbook ed. Walter Powell (New Haven: Yale University Press, 1987), pp. 99-117.

5 Sanford Borins, "Privatization Theory and Practice," a review of T.M. Ohashi, and T. P. Roth, Distributing Shares in Private and Public Enterprises, in Canadian Public Administration 24 (1981) pp. 143-145.

6 Ruth DeHoog, Contracting Out For Human Services: Economic, Political, and Organizational Perspectives (Albany, New York: State University of New York Press, 1984).

7 Mark Schlesinger, "Competitive Bidding and States' Purchase of Services: The Case of Mental Health in Massachusetts," unpublished paper, JFK School of Government.

8 Spitzer and Scull, "Privatization and Capitalist Development."

9 Charles Hoch, "Municipal Contracting in California: Privatizing With Class," Urban Affairs Quarterly 20 (1985) pp. 303-323.

[10] Barbara Stevens, editor, Delivering Municipal Services Efficiently: A Comparison of Municipal and Private Service Delivery, A technical report prepared for the U.S. Department of Housing and Urban Development (New York: Ecodata, Inc., 1984).

[11] Stevens, Delivering Services, ii.

[12] Stevens, Delivering Services, 8.

[13] The survey is a pilot study for a larger four-state project which NIMH has approved but not yet funded due to budget delays. A copy of the questionnaire and interview schedule are available from the author upon request.

[14] Carol DeVita and Lester Salamon, "Commercial Activities in Human Service Organizations," in The Constitution and the Independent Sector: 1987 Spring Research Forum Working Papers (Washington D.C.: The Independent Sector, 1987).

[15] John Lammers, "Competition and Personnel Practices Among Nonprofit Organizations" paper presented at the Annual Meeting of the Society for the Study of Social Problems (April 9-12, 1987) Atlanta, Georgia.

[16] DeVita and Salamon, "Commercial Activities."

[17] Some curtailed federal funds were passed through county programs--a source of considerable confusion to respondents and complexity to managers.

[18] This is consistent with findings reported in studies of other cities, for example, by Diane M. Disney, Madeline H. Kimmich, and James C. Musselwhite Partners in Public Service: Government and the Nonprofit Sector in Rhode Island (New York: The Urban Institute, 1984) and by Kirsten Gronbjerg, Hardship and Support Systems in Chicago (New York: The Urban Institute, 1987).

WORKING DRAFT

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THE FUTURE OF PUBLIC/PRIVATE PARTNERSHIPS: LESSONS FROM A LOCAL GOVERNMENT HEALTH AGENCY

by

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The views expressed here are those of the authors and do not necessarily reflect the views of the Fairfax-Falls Church Community Services Board, its Board members, or staff. The authors wish to express their appreciation to the Community Services Board staff and to other key informants listed at the back of the paper. We especially wish to thank Joan Durman, Director of Planning and Management Analysis at the Fairfax-Falls Church Community Services Board, for her review of this paper and for her helpful suggestions.

By now much has been written on public/private partnerships from the perspective of studies focused on communities and particular human services sectors.[1] Such work has been crucial to an understanding of public/private partnerships but, like any approach, this work has limitations. In particular, this approach neither provides policymakers with a clear distinction between general patterns and operations at the agency level nor with recommendations based on an agency's perspective. The primary purpose of this paper, therefore, is to integrate a particular agency's experience into broader policy analysis in order to help decisionmakers think more concretely about the future of public/private partnerships.

This paper is organized into four sections. The first describes the local government agency context. The second analyzes the major policy issues of concern. The third outlines the principal contracting choices faced by the local government agency and recommends how these choices might be made. The last section relates the agency's experiences to broader implications for the future development of public/private partnerships.

THE CONTEXT

The local government health agency serving as the focus of this paper is the Fairfax-Falls Church Community Services Board (CSB), which was created in 1969. The CSB is empowered by state code to plan, provide, and monitor mental health, mental retardation, and alcohol and drug abuse services for a population of approximately 720,000 people in Fairfax County and the independent cities of Fairfax and Falls Church, Virginia in suburban Washington, D.C. [2] Fairfax County government is the fiscal agent for the CSB, requiring the CSB to follow all county administrative and personnel procedures. The CSB's FY1988 budget is $35 million. Staffing includes 592 full-time equivalent merit positions and 19 full-time equivalent contract positions for the provision of outpatient, emergency, day support, residential, and other services. In addition to the services provided by these employees, the CSB also contracts for services with 26 private, nonprofit agencies, two for-profit agencies, and two government agencies.

Decentralization

Shifting human services responsibilities from the national level to state and local governments has been a major federal priority in the 1980s. At the CSB, however, the move toward decentralization began even earlier. Federal funding for CSB activities declined substantially before the Reagan administration because of the scheduled "step down" in federal funding for the CSB's three community mental health centers. The CSB was well equipped to deal with this federal retrenchment in ways that many of its counterparts were not when the Reagan initiatives in human services were first implemented in the 1980s. Two factors stand out. First, the CSB is governed by a Board of 15 citizen volunteers, who are appointed by local elected officials and are very active in community affairs. This keeps the CSB in tune with local needs and provides the CSB with a built-in capacity to mobilize political and policy support for its programs. Second, local government is both willing and able to support human services programs. As shown in Figure 1, 60 percent of CSB funding comes from local government. This degree of local support is unique among Virginia's 40 Community Services Boards. Combined with state support and client fees, 91 percent of all revenues come from non-federal sources.

Privatization

The 1980s have focused much attention on the privatization of public services. The actual impact is debatable, however, in large part because public agencies were already contracting for services before privatization was "discovered." The CSB, for example, began the 1980s already channeling just under one-fifth of its budget to nonprofit agencies. As the CSB budget grew rapidly in the 1980s, the share of funding contracted to nonprofit agencies increased slightly to 21 percent by FY1987. This indicates that the CSB maintained its commitment to public/private partnerships in the decade but did not greatly increase them in response to privatization rhetoric.

How does this level of CSB contracting compare to human services contracting elsewhere? The evidence available indicates that the CSB does not contract as extensively as do its counterparts in other communities. This is particularly evident in mental health and alcohol and drug abuse services, both of which contract less than 15 percent of their CSB expenditures (see Figure 2). Nonprofit Sector Project data for 1984 show that about half of these services were contracted in its national sample of 16 communities.[3] Interviews with government and private informants in other communities confirmed the CSB's overall low level of contracting for services.[4]

CSB contracting is heavily concentrated in one service area - day support. The private sector has developed a wide variety of high quality services for sheltered workshops, vocational training, supported employment, psychosocial treatment, and day activities that are responsive to the diverse requirements of CSB clients. Because of the availability and quality of these services, there is no need to provide most of them in the public sector.

CSB contracting for services other than day support is very limited. Greater contracting for these other services nationally suggests that either the CSB is not contracting as much as it might usefully do or that there is something decidedly different in the CSB's orientation toward contracting for services. The fact that neighboring jurisdictions in Virginia and Maryland contract substantially for similar services offers additional support for these hypotheses.

POLICY ISSUES AND ANALYSIS

To examine contracting possibilities across all CSB programs is beyond the scope of a single paper. Because the CSB's most pressing program development and management issues are in residential services, the focus of the remainder of the paper will be residential programs. The CSB will continue to face major residential programming issues well into the next century because the demand for these services is so great, costs so high, and services so complex and differentiated. The challenge is to expand services as rapidly as possible, but in a way that leads to sound and long-term development of a comprehensive residential system.

For those not familiar with such programs, it is important to keep in mind that residential programming is far more than shelter. CSB residential programs include combinations of support services, psychosocial therapy, training, counseling, life skills, and transportation services which vary greatly according to the needs of clients. Programs are arrayed across a continuum including emergency or crisis residential facilities, group homes, apartments, and support services for persons living in their own homes. In FY1987, the CSB funded 407 residential beds, 77 of which were contracted to nonprofit agencies as shown in Table 1. In budgetary terms, 14 percent of residential services were contracted to nonprofit agencies as shown in Table 2.

Exact figures were not available, but respondent information suggests that other communities contract for residential services to a greater extent than does the CSB. In fact, the CSB appears to be one of the few large systems nationwide that provides the bulk of residential services by using public employees. In some states such as New York and California, virtually all residential services are provided by the private sector.

Current Residential Issues

Three major issues were identified for CSB residential programs during the course of this work and include the need for:

- Increasing flexibility in program operations,
- Expanding services, and
- Building greater community support.

Interviews with CSB staff indicate that the major problem with its publicly operated residential services is the lack of flexibility in operating programs. For example, Fairfax County personnel practices usually take three months to hire staff. Because staff turnover can be high in these programs, staff positions are perpetually underfilled, and overtime hours and stress are often very high. County purchasing requirements also make it difficult to buy items and services in a timely manner; as a result, the quality of the home environment for residents is sometimes diminished. County maintenance of buildings and grounds is also problematic, often causing the major obstacle to community acceptance of residential programs.

Apart from the need for more flexibility, the CSB is also faced with an almost unlimited need to expand the volume and types of residential services available to its clients. Although the number of residential beds has increased significantly in the 1980s, more than 1,000 additional persons, most living with their parents, are known to need these services today. As their parents age and die, considerably more disabled adults will need these services in the future. Even if funding were available, it is unlikely that the CSB would want to provide all these residential services through the public sector. Such expansion of directly operated residential programs could lead to an unwieldy bureaucracy. Moreover, elected officials might be uncomfortable with so many additional public employees.

A major concern of any residential program is community support and acceptance. In Fairfax County, most communities have covenant restrictions that make the location of residential programs difficult. [5] High real estate values and low vacancy rates further complicate the process. Starting a new program or relocating an existing one is a lengthy and expensive process, fraught with possible political repercussions. Though the CSB has been generally successful in developing needed community support, considerable effort has been required to encourage and maintain this support.

Contracting As A Solution

Does contracting offer solutions to the major residential issues facing the CSB? Though not a panacea, increased use of nonprofit agencies offers residential alternatives to program management. There are trade-offs, however, as discussed below.

Flexibility. The greatest advantage to the CSB of contracting residential services is increased flexibility. CSB decisionmakers are already aware of this advantage. This aspect of contracting out is almost always a major factor discussed in the literature, and most respondents in our interviews cited flexibility as a reason to privatize services. [6]

In addition to more responsive operating procedures, nonprofit agencies also offer another aspect of flexibility. Because they tend to be smaller and community-based, nonprofit agencies may be able to offer more diversity than the public sector in providing services. This is particularly true if services can be customized to better satisfy community and client values whether they be cultural, neighborhood, or other values. [7]

Program Expansion. If a significant expansion of CSB residential services occurs within the next decade as projected, private agencies will almost certainly be needed to help plan and staff some of them. The magnitude of funding and clients will require making use of all community resources to bring programs on line. Though not generally recognized, rapid human service development in this country has been associated with expanded use of nonprofit agencies because it is often easier and quicker to start programs through the private sector. 8/ Because most communities prefer to limit the growth of government, contracting is often an alternative to permit program expansion that would not otherwise be possible.

Apart from sheer numbers, nonprofit agencies may make significant contributions through specialization. As the service continuum broadens, the CSB may find it most efficient not to expand its own direct services where nonprofit agencies develop expertise. Nonprofit agencies may also be program innovators in a service field forever being innovated. 9/. At a minimum, public and private sectors can do things differently and thereby stimulate greater program development.

One advantage of contracting is often assumed to be a reduction in the cost of services. Pinning down cost comparisons is very difficult, but the data available yield ambiguous results. A contract that at first seems to be a cost savings arrangement may, on closer examination, turn out to reflect only part of the costs of the service. The total costs of a contracted service must also include public sector costs for overseeing the proper usage of public funds. The CSB, for example, spends a considerable amount of money on contract management which is not immediately apparent. CSB staff also develop and evaluate RFPs, provide considerable technical assistance in program development and financial accounting, and monitor program and fiscal operations.

One reason that nonprofit providers are thought to be less expensive than government providers is that they may have lower labor costs and receive private contributions. This view may be problematic, however, for two reasons. First, lower wages in the voluntary sector often mean higher turnover in staff and a lower level of professionalism. These outcomes may diminish the quality of service provision. CSB experience suggests that comparable wages are necessary to develop a similar quality of services in both sectors. Second, both government and nonprofit agencies receive volunteer time and donations. 10/ As a result of these factors, it is far from clear that privatizing residential services will reduce their total costs over the long run. 11/

Community Support. Nonprofit agencies offer the CSB an important avenue for increasing community support for residential programs. A community residence operated by a nonprofit agency may appear less of a threat to a community than one run by a large county agency. Nonprofit agencies may also educate parts of the community the CSB cannot reach and effectively advocate for client needs in ways that a public agency cannot. In some cases, nonprofit agencies may be better able to deflect political criticism than could the CSB. At a minimum, the use of nonprofit agencies extends the network of human service supporters.

Trade-Offs

As with any real-life alternative, contracting advantages come with a set of trade-offs. Three major ones for the CSB are loss of control of programs, difficulty in placing the most demanding clients, and the potential failure of private programs.

Loss of Control. In the mind of the public administrator the principal disadvantage of privatization may be the loss of control. A certain amount of lost control over program design and implementation is inevitable if the private agency is to be more flexible, innovative, and community-oriented than a comparable government agency. On the other hand, private agencies also must give up some control in public/private ventures. Well-written contracts and good monitoring procedures can ensure that the public interest is served and also provide private agencies with clear operating parameters.

Difficulties Placing Clients. A major CSB concern in contracting services is the difficulty in placing severely disabled clients in private agencies. The CSB has experienced these difficulties because private agencies have not always been capable of serving very disabled clients or because agencies have feared assuming the financial or legal responsibilities such services entailed. Severely disabled clients are served by private agencies in many communities, however, though a number of respondents interviewed did cite difficulties in this area. One private provider suggested that large, sophisticated private agencies are competent to provide intensive services and do so where contracts build in the true cost of service.

The Failure of A Private Program. An important concern for any public agency is what to do if a private agency fails financially or is found to provide grossly incompetent services. Canceling a contract is not an adequate solution for a residential program failure because it places disabled clients on the street. The impact of failure is thus far greater than in most other contract services.

Form of Contractual Arrangements

The CSB has two major forms of contractual arrangements in residential services. The first is a typical contract arrangement in which the CSB pays the full costs of client services as negotiated in a purchase of services (POS) contract. In FY1987, this method was used to contract for 67 beds. The second type of contractual arrangement in residential services is called a "public/private partnership." In this contracting mechanism, the CSB and the nonprofit agency each pay 50 percent of costs. The "public/private partnership" program was established to expand services to high-functioning disabled clients who need residential services but are not the highest priority clients on the public sector waiting list. The program began in mental retardation and is being expanded to include mental health. In FY1987, two group homes with a total of 10 beds were in this program. Review of the literature and interviews suggest that this contract arrangement may be unique to the CSB. 12/

Though the "public/private partnership" program creates many new opportunities for service delivery, it also raises two major concerns. First, will the 50 percent private match continue into the future? Currently the CSB does not have enough information on client needs and family financial resources to make ten-year projections of the stability of the private match. Projections of this length are needed if the CSB is to continue expanding these programs. A second major concern is that the distinction between "public/private partnership" and standard purchase of service agreements be maintained. This is important to ensure that private matches continue to be directed where public agency resources are most limited.

CONTRACTING CHOICES AND THE FUTURE

Analysis of CSB residential issues and contracting suggests that increased privatization may play a vital role in meeting future residential challenges. Policy recommendations are needed, however, to help CSB decisionmakers determine when to contract. Such recommendations can provide guidance on how to decide but cannot provide formula criteria on what to decide. That responsibility must remain with the program decisionmakers, who are closest to individual situations and accountable for the expenditure of public funds.

Key Factors to Consider

There are three factors that merit special attention in CSB contracting for residential services.

Provider Policy. Based on its own experience and that of other communities, the CSB should develop residential policies stating which types of services are best contracted. Because of the severity of need, the CSB must always be prepared to serve directly the most disabled clients and those in crisis when no other providers can be found. Service for these clients can be contracted, however, when providers are available and possess sufficient expertise. Some severely disabled CSB clients are already being served through POS agreements. POS contracts are also appropriate for less impaired clients. "Public/private partnerships," by contrast, should continue to serve only high functioning clients. This is necessary to leverage private dollars for providing services to those clients who would not otherwise be served.

Speed of Implementation. A very attractive characteristic of private agencies is that they are often able to start a new program more rapidly than a public agency. While advantageous, CSB decisionmakers should resist contracting out based solely on speed of implementation. Rather they should also consider the private agency's capacity to provide quality services. If contracting with a nonprofit agency is required because of the need for speedy implementation, program decisionmakers must examine the long-term consequences for the availability and quality of services. If necessary, the CSB must be prepared to provide technical support to develop the nonprofit agency's expertise or to change service providers in the future.

Specialization. Program decisionmakers should periodically assess the ability of nonprofit agencies to specialize in providing certain types of services or to serve certain groups of clients. For example, nonprofit agencies may specialize in apartment programs or services to the elderly or minorities. The CSB may particularly wish to encourage nonprofit agencies to serve groups it has had difficulty in reaching.

How Much Contracting?

There is no fixed percentage of services that should be contracted at the CSB or elsewhere. Rather than trying to establish or reach some fixed contract share, CSB decisionmakers should focus only on contracting to enhance the quality and availability of services.

The Pace of New Contracting

The pace of new CSB contracting generally should be gradual rather than abrupt. Adding five contract programs over five years is preferable to adding five the first year. Moving abruptly to contracting places considerable strain on resources for RFP and selection mechanisms, technical assistance, and contract management. For an agency where residential contracting has been limited, these mechanisms may be inadequate in the short-term if overloaded.

Special Considerations

There are three contract issues of special consideration for CSB residential contracting.

Structural Change. If the CSB decides to contract for residential services to a substantial degree in the future, it will need to change and augment its own organizational structure. In particular, the CSB will need to have formal contract managers in each program area and inventory its contract management training needs. The CSB will also need to evaluate its current quality assurance mechanisms to ensure that they are appropriate for a much larger private sector role.

Ownership of Assets. A major issue for the CSB is the ownership of assets, primarily the land and buildings of residential programs. Property values are high in Fairfax County, but restrictive covenants and the community review process make residential program land and housing even more valuable to the CSB. The CSB should have an operating policy of either owning or holding the lease on group homes managed by private agencies. Exceptions may be granted for historical reasons or when such housing is paid for entirely by private funds. This will enable the CSB to continue to use the facilities if the contractor becomes unable or unwilling to provide services.

Private Failure. If the CSB substantially expands its reliance on nonprofit agencies, the probability of a private program failing will increase. Well written contracts and good contract management, however, should give the CSB ample warning of major problems before they occur. If major problems point to failure, the CSB will need to establish agreements with other contractors or take over the service itself.

The CSB needs to develop more front-end technical assistance for long-term funding in its "public/private partnership" programs to prevent failures. This may include strategies for creating endowments, for having parents' wills written to support their children, or for developing profitable enterprises to generate program income. Emphasis should also be placed on selecting high functioning clients who can transition to independent apartment living after three to five years in the program. This will minimize long-term dependence on resources from the same set of families. At the same time, ten-year profiles for each program need to be developed to match client costs to available revenues. If a short fall should be expected, the CSB may need to consider a reduction in the share of private match funds.

CONCLUSIONS AND IMPLICATIONS

There are a number of broader policy implications raised by the CSB experience. One is the relationship of political culture and government's use of private service providers. 13/ Nonprofit Sector Project data suggest that extensive public/private partnerships are associated with more established and heterogeneous populations often found in the Northeast and Midwest. The CSB's neighbors in Arlington, Virginia and nearby Maryland communities are also fairly established, heterogeneous areas where contracting for services is high. The Fairfax-Falls Church area, by contrast, is more similar to rapidly growing areas in the South and West where contracting for services is often lower. 14/ Comparing the development of residential programs in communities with and without major traditions of contracting should offer important insights into the role of political culture, specialization, and small scale service provision in determining public/private cooperation. What is really different about Fairfax County, Virginia where contracting is minimal and Westchester County, New York where contracting is substantial? Will Fairfax become more like Westchester as it "matures?" Or are other factors more important—state versus locally administered systems, legal decisions, or variations in civil service rigidities?

A second point raised by the CSB experience concerns the nature of community residential programming. The small scale of services, their complexity, and the fact that services are community-based suggests that public/private partnerships should be extensive in this field. 15/ If privatization does not increase as these services expand nationally, a number of hypotheses about contracting need to be re-thought. One interesting point to be explored is the relationship between public agencies with citizen boards like the CSB and their propensity for contracting services. It may be that "community-based" public agencies are either better able to provide these services directly or are less willing to contract for them.

At the broadest level, the CSB experience suggests that it is crucial to examine America's suburban communities to understand the future of public/private partnerships in this country. In many respects, the history of public/private partnerships is a city history, the tradition of which enriches suburban areas as well. This can be seen in government and private cooperation in the large medical complexes, universities, museums, innovative human services programs, and cultural jewels of our cities. Yet the future development of human services partnerships is likely to be more heavily influenced by suburban needs, preferences, and environments. A larger share of people now live and work in suburban communities than in the cities, and the relative importance of suburban areas is likely to continue to grow. Researchers and policymakers alike need to give more thought to the suburban dynamics of future public/private cooperation.

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NOTES

1. The Nonprofit Sector Project work at The Urban Institute provides the most comprehensive and intensive examination of public/private partnerships at the community level. For a summary of this work, see James C. Musselwhite, Jr. and Lester M. Salamon, "Changing Public/Private Roles In Human Services", a paper presented at the Independent Sector's Spring Research Forum (March, 1987). A sector study of relevance to this paper is James Ferris and Elizabeth Graddy's, "Sector Choice For Local Health Contracts: Public, Nonprofit, or For-Profit?" School of Public Administration, University of Southern California, July 10, 1987.

2. The population of Fairfax County has grown from just under 100,000 in 1950 to nearly 700,000 today - the same size as the City of San Francisco. The independent cities of Fairfax and Falls Church are older, more stable communities with a combined population of about 30,000.

3. Unpublished data from The Urban Institute's Nonprofit Sector Project cited by permission.

4. A list of individuals interviewed for this paper appears at the end of this section.

5. Approximately 72 percent of Fairfax County subdivisions contain restrictive covenant language that may be used to prevent a group home from opening in a neighborhood.

6. This and other advantages of contracting out are discussed in Harry P. Hatry and Carl F. Valente, "Alternative Service Delivery Approaches Involving Increased Use of the Private Sector," The Municipal Year Book 1983 (Washington, D. C.: International City Management Association, 1983), pp.199-217.

7. Ralph M. Kramer, Voluntary Agencies in the Welfare State (Los Angeles: University of California Press, 1981) discusses the extent to which greater heterogeneity of values appears to lead to greater use of nonprofit agencies.

8. James C. Musselwhite, Jr. and Lester M. Salamon, "Social-Welfare Policy and Privatization: Theory and Reality in Policymaking," in Mark S. Rosentraub (ed), Urban Policy Problems: Federal Policy and Institutional Change (New York: Praeger, 1986), pp. 65-87.

9. In New York City, for example, nonprofit human service agencies pre-dated government agencies and have continued to be a major source of innovation. See Alan J. Abramson and Lester M. Salamon, Government Spending and the Nonprofit Sector in New York City (Washington, D.C.: The Urban Institute Press, 1986), pp. 35-38. For the Fairfax-Falls Church area the private sector has been an innovator in psychosocial services for mentally ill clients, day support for mentally retarded persons, and residential programs for substance abusers.

10. Donations to the CSB of furniture, lawn mowers, personal computers, and even cash are not uncommon. Donors provide residential facilities with items they might not otherwise get and provide them more quickly.

11. The literature generally assumes that contracting reduces cost. Empirical studies of the assumption, however, have lead to ambiguous results. See Ferris and Graddy, op. cit., pp. 4-8, for a discussion of some of these issues. Conversion of existing government services to private operation is actually more expensive in the short run than maintaining government services. See The Feasibility of Contracting in Virginia's Mental Health and Mental Retardation Facilities (Richmond: Virginia Department of Planning and Budget, March, 1987).

12. In the Phoenix area, residential services for mental health are based on a matching program, but the private match is considerably lower and is renegotiated periodically based on the availability of private funds.

13. For an empirical demonstration of important differences in political culture at the state level see Robert S. Erikson, John P. McIver, and Gerald C. Wright, Jr., "State Political Culture and Public Opinion, "American Political Science Review, Volume 81, Number 3 (September, 1987), pp. 797-813.

14. For a discussion of contracting human services in two such communities see James C. Musselwhite, Jr., Lester M. Salamon, John J. Hall, and Pamela Holcomb, Human Services Spending in Phoenix and Pinal County: The Changing Roles of Government and Private Funders (Washington, D. C.: The Urban Institute, 1987)

and Mark S. Rosentraub, Pamela A. Holcomb, Lester M. Salamon, and James C. Musselwhite, Jr., Human Services Spending In Dallas: The Changing Roles Of Government and Private Funders (Washington, D. C.: The Urban Institute, 1987).

15. For a discussion of various theories of public/private partnerships, see Lester M. Salamon, "On Market Failure, Voluntary Failure, and Third Party Government: Toward A Theory of Government-Nonprofit Relations In the Modern Welfare State," Journal of Voluntary Action Research, Vol. 16, Numbers 1 & 2 (January - June, 1987), pp. 29-49.

Persons Interviewed For This Paper

Fairfax-Falls Church Community Services Board Staff

William Benton, MAXIMUS, Fairfax County, Virginia

Valarie Bradley, The Human Services Institute, Cambridge, Massachusetts

Paul Carling, Center for Community Integration, University of Vermont, Burlington, Vermont

Lin Corbin-Howerton, Virginia Department of Planning and Budget, Richmond, Virginia

Joni Fritz, National Association of Private Residential Resources, Falls Church, Virginia

Harry P. Hatry, The Urban Institute, Washington, D. C.

Sharon Kelso, United Community Ministries, Alexandria, Virginia

Harvey McConnell, Pathway Homes, Fairfax, Virginia

Gloria Merk, Developmental Services State of California, Sacramento, California

Richard Ridenhower, formerly of the Department of Health, Marin County, California

Nancy Rosenthal, Arlington Community Services Board, Arlington, Virginia

Jay Roundy, TriCity Behaviorial Health Center, Mesa, Arizona

Russy Sumariwalla, The United Way of America, Alexandria, Virginia

Barbara Todd, former Board Member of the Fairfax-Falls Church Community Services Board, Falls Church, Virginia

Alfred Tuttle, New York State Conference of Local Mental Hygiene Directors, Albany, New York

Carol Whitcomb, Community Services Systems, Fairfax County, Virginia

TABLE 1

COMMUNITY SERVICES BOARD RESIDENTIAL BEDS, FY1987

Program	Total Beds	Beds Contracted To Nonprofit Agencies
Mental Retardation	138	24
Mental Health	162	32
Alcohol and Drug Abuse	107 1/	21 2/
TOTAL	407	77

Source: The Fairfax-Falls Church Community Services Board

1. Certain types of residential services are contracted as resources permit. These contracts are for client days with both public and nonprofit providers. In FY1987 these contracted services were equivalent to approximately 31 beds.

2. Residential contracting to nonprofit agencies amounted to the equivalent of 21 beds in FY1987.

TABLE 2

COMMUNITY SERVICES BOARD SPENDING AND NONPROFIT CONTRACTING FOR RESIDENTIAL SERVICES, FY1987

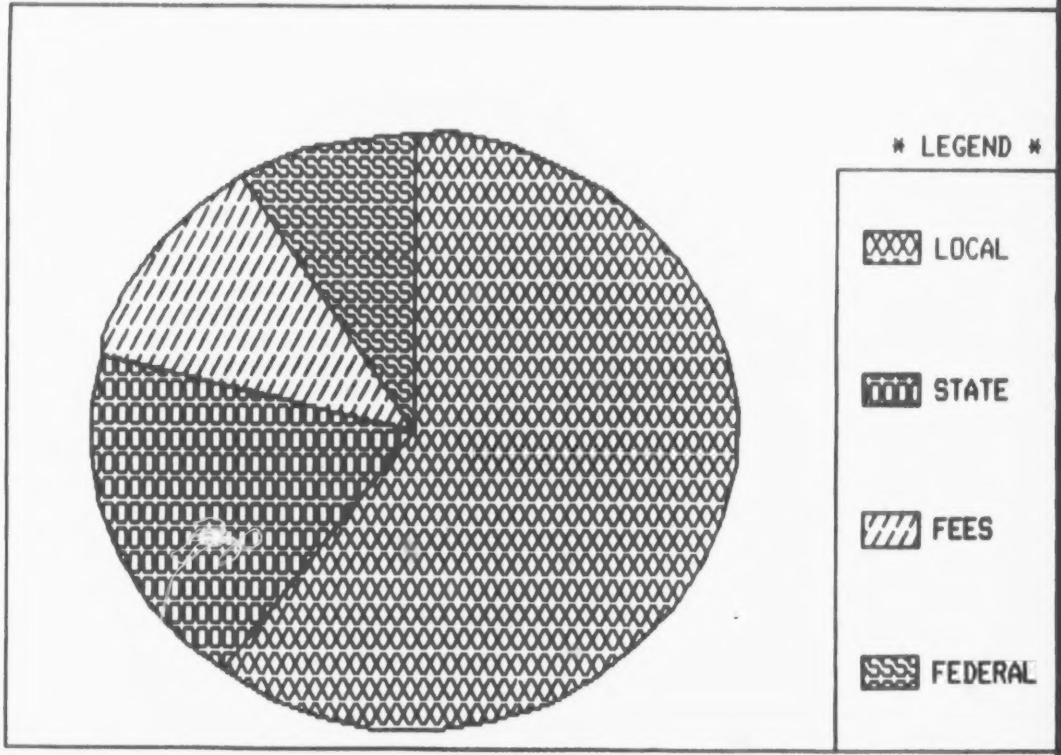
Program Area	Total Residential Expenditures	Percent To Nonprofit Agencies
Mental Health	$3,615,846	12 %
Mental Retardation	$2,476,926	15
Alcohol and Drug Abuse	$1,434,193	17
TOTAL	$7,526,965	14 %

Source: The Fairfax-Falls Church Community Services Board

FIGURE 1

SOURCES OF COMMUNITY SERVICES BOARD FUNDING

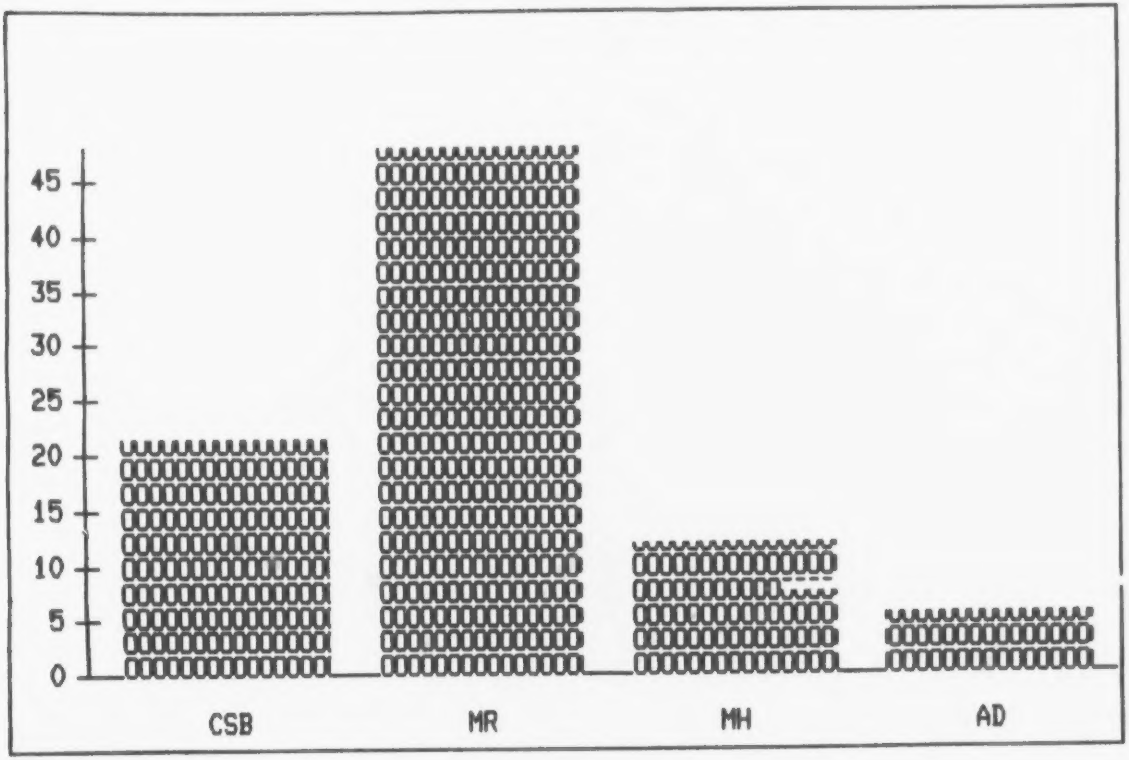
FY1987



SOURCE: The Fairfax-Falls Church Community Services Board

FIGURE 2

PERCENTAGE OF COMMUNITY SERVICES BOARD FUNDING CONTRACTED WITH PRIVATE, NONPROFIT AGENCIES, FY1987



CSB: Community Services Board
MR : Mental Retardation
MH : Mental Health
AD : Alcohol and Drug

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SOURCE: The Fairfax-Falls Church Community Services Board

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REGIONAL GENEROSITY AND CIVIC COMMITMENT

by

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INTRODUCTION

Under the right set of circumstances ample *private generosity* could provide for the well being of all those needing assistance anywhere and to improve the amenities and quality of life of our own and more distant communities. But because circumstances have never been "completely ideal everywhere," the United States slowly developed and refined a *state* concept of entitlements, equitable access, and social justice, creating a system of *public* generosity at national, state and local levels. As a result, Americans have a dual and specialized system of private and public generosity but very diverse notions remain about the locus of responsibility for the poor and handicapped as well as gifted students and opera lovers.

From a national perspective, *private* generosity now tends to specialize more and more at the local community level and to support chiefly those in-kind services with a narrow social gap separating donors and beneficiaries (with some notable exceptions). Private generosity has shifted from a traditionally more *charitable* and pervasive role to this more local and specialized *membership* and *philanthropic* focus. This shift has been so extensive that it may not be possible (with less public generosity especially at the federal level) to restore local private or public charity and responsibility *everywhere* to its traditional and more comprehensive functions? [see Salamon; Steinberg]

The broadening federal role in the past fifty years, albeit with some occasional reluctance and reversals, has been the major new element in enhancing national thresholds and safety nets of service provision. This expansion of public generosity has extended to beneficiaries nationally many of the progressive programs of the more generous states and localities. The present decentralization trend moves us nationally closer to levels supportable by the more traditional and parsimonious communities. The persistent differences in local and state public as well as private efforts, the subject of this paper, provide some hint about the distributional consequences of greater or lesser federalism.

Local and Regional Values

The apparent displacement of local generosity is likely to be a biased view taken only from the national perspective. Private generosity has still been engaged (but in some places more than others) in its traditional role of blending charity (i.e. transfers to the poor) with philanthropy (i.e. support for institutions providing services of merit.) In fact, a plausible case also can be made that local philanthropy has been influential in bringing about local public support for the same social, health, educational, and cultural institutions and amenities that are recipients of private giving. Private and *local* public (and in many cases, state) generosity are consistent and move in tandem but are unequal between places.

This formulation presumes that both private and public generosity are rooted in community and pluralist standards [Katz]. Private and public generosity expressed at the community level should be parallel indicators of the same underlying ideological base. Generosity is not an isolated characteristic but has other expressions in moral and social attitudes and practices and in civic commitment that differ significantly between communities. There are generous and parsimonious communities.

Pluralism and Federalism

In fact, the federalism-pluralism framework that seems to provide the best fit to the decentralization process has a distribution of highly stable regional symbols of political altruism and generosity expressed by the social policies of our American states and localities, a Massachusetts or Minnesota progressivism, a South Carolina traditionalism, and the Texas free-riders. Meanwhile, the federal government is quite skittish, vacillating in its stance initially like the extreme states and then the compromise places, shifting from an Ohio to a California and then back to a New Jersey.

This approach is simplified, of course, but is likely to have some validity because federal initiatives typically imitate policies initiated and tested at state and local levels. National adoption of regional and local ideas about many welfare and social and health services occurs after some lag and with the urging of Congress, and lobbyists, think tanks, and public action groups with a local and comparative perspective.

But the federal extensions and contractions of these entitlements and service programs are not implemented uniformly over the nation. Thus, conservatives and progressives as well as free-riders all develop reasons to become disappointed. First, the federal dollars in the progressive places only supplement but they do not make redundant or substitute fully for state and local expenditures for social, educational, cultural, and health services. Residents of these places now have local and state (as well as philanthropic) help to support their generous concepts of equity, amenities and quality of life. The irritant, however, is the additional federal tax that must be levied throughout the nation for transfer to the conservative and free-rider places to support the new federal standards. Extending local concepts of generosity to the entire nation seemed like a good idea provided that the idea and practice of a "fair share" of support would catch on everywhere.

The progressives have been impatient to promote national adoption of their fair share standards and invented matching grants to reinforce the "proper habits" and formulas for block grants to target the deserving. They created organizations like the Advisory Council on Intergovernmental Relations (ACIR) which monitor state and local tax "effort" that can be used alongside measures of "fiscal capacity." Their findings and diagnoses are like the report card messages school children receive, "needs more (fiscal) effort, not working up to (tax) capacity, and not sharing or playing fair." When free riders don't begin taxing themselves to contribute their fair share, liberals tend to lose heart and accede to the retrenchment forces. Innovativeness and generosity are certainly not lacking in selected communities and state capitals but it is the values and policies of the more conservative and free-rider states that are likely to be most instrumental in the national pursuit of centralization or decentralization.

Voters in the free rider places have mixed feelings about accepting the federal largesse. Increases in federal support for mailbox income or services could raise expectations and attract or prolong the residency of poor people less inclined to stay on the basis of state and local aid alone. What would be the local tax and charitable burden if federal aid were to be curtailed? Genuine traditionalists believe that parsimony is a virtue and people must learn self- reliance and are harmed by generosity.

Study Design

The major elements and assumptions of this regional perspective can be tested. The framework assumes, for example, that: generosity can be measured and assessed comparatively after making proper allowance for differences in community resources and of distress; patterns of regional generosity exist and have some stability; and public and private expressions of generosity at least at state and local levels are consistent and move in tandem rather than displacing one another.

The opposing viewpoint would suggest that generosity as a moral gesture cannot be distinguished from the cultural expression of tastes and values (e.g. Gotham has no ballet or community mental health facilities because of cultural preferences and not due to lack of generosity.) The community differences could be merely a reflection not of generosity but of tastes and preferences that vary between regions, or between their cultural, ethnic or religious groups. The absence of any particular service could mean simply that local residents do not value its provision or they have an adequate substitute.

Furthermore, how can private generosity, charity and philanthropy which is altruistically motivated and voluntarily given be equated with public sector expenditures for transfers and services that are supported through a coercive system of taxation? Additionally, how can stability in regional patterns be sustained with the continuing migration of people and jobs, the strong pressures for national homogenization of social values, and the almost universal civic competition between places to improve their reputation for amenities and quality of life?

THE MEASUREMENT OF GENEROSITY

The term generosity implies giving behavior prompted by mixed rather than solely altruistic motives. Recipients (e.g. users of subsidized services) are likely to benefit while donors may or may not benefit directly or indirectly from the donation. In contrast, a true gift implies asymmetry and no reciprocity as exemplified by an activity that benefits only future generations or places or social groups too distant to reciprocate [see Ball]. Charity generally refers to gifts that span a considerable social gap, while philanthropy involves substantial support for institutions that provide worthy services or work toward solving significant societal problems.

Private Generosity

Existing secondary or panel data do not, however, allow us to distinguish true gifts, charity, and philanthropy. One can only measure the flow of funds (and some volunteer labor) to not-for-profit organizations that provide services and are eligible to receive tax deductible donations. In a gross way, one can suggest that donations targeted for social and welfare services are likely to be more "gift-like" and asymmetrical than those supporting cultural, hospital and educational institutions. Little detailed study has been made, however, about reciprocity or redistributive effects of various types of donations in different locales. Furthermore, virtually nothing is known about donor-beneficiary relationship in religious giving that constitute almost half of all donations. Disaggregated information is also lacking about funds raised in the national "disease" campaigns and for overseas relief, some portion of which must be classified as true gifts.

Private generosity is then the more inclusive term for the composite of donations that support services and extend their provision with some subsidy to those the community agrees can benefit. Since the overwhelming proportion of giving is extended within the same community for current service use by the donors themselves or others not so different in social class, such generosity is not primarily a true gift or even charity or philanthropy but largely a contribution to civic or community quality of life or improvement (i.e. amenity supporting.)

Public Generosity

The equivalent notion of local public sector generosity also involves subsidy to support amenities and extend their relative scope and quality beyond the "usual" public service levels to be expected in a community of that size and resources. The pluralist American tradition, however, is to regard federal or national efforts at social justice and reduction of disparities as coercive, the payment of local taxes as a form of membership dues or generosity; and to assign a flexible and shifting role to state government. We are apparently willing to regard the equitable distribution of income and access to basic services as a national public good to be supported principally by taxes on income. But we are reluctant (but more so in some places than others) to support such transfers through taxes on property, the main base of support for municipal government. Thus, an expanded federal role should have a differential role in displacing local public and private generosity depending upon local initiatives and division of functions [see Salamon; Steinberg].

The Generosity of Places

We generally think of generosity as an attribute of individuals or groups but the focus here is on places. Generous communities then are those which make substantial public and private efforts within their means and preferences to provide a wide range and high quality of affordable services [Wolpert]. Generous communities are somehow able to solve their "free rider" problem by arousing altruistic feelings or civic pride or by creating services of direct or indirect benefit to donors and tax payers. Their residents manage to donate part of their income or wealth and/or tax themselves to expand service provision and make these services available to those who would otherwise be excluded. Those favoring lower taxes and more modest public expenditures for services than the prevailing community preferences have presumably moved to places with like-minded residents. Residential and siting decisions by households and firms reflect at least partially the attraction of amenities and their "tacit agreement to be taxed" for public as well as charitable services.

Why should some places be more generous than others and why should these distributional patterns have some stability over time? Theory based primarily upon median voter motives for giving would lead us to expect that private and public generosity levels would be higher in the smaller, more affluent, and more homogeneous metropolitan areas with relatively low levels of distress [see Buchanan]. Giving rates and support for amenities according to this approach should be predictable from income and wealth distribution.

In contrast, theory based upon a Tiebout framework would suggest residents and firms sort themselves by region according to preferences for levels of services and amenities and willingness to tax themselves privately and publicly to underwrite their costs [Tiebout]. According to this approach, areas similar in social and economic composition could differ considerably in generosity and amenity levels. The regional expressions of cultural values, traditions, and institutions should be reflected in the amenities and quality of life that residents are committed to support. These alternative approaches require further specification and testing.

Intervening Targets and Competing Donors

Local giving targeted to social services could be vulnerable to displacement by federal contributions and potentially offset by the competing solicitations from local health, education, and arts institutions. The decision problem for donors is analogous to the crowding out framework of Stouffer's "intervening opportunity" and "competing migrant" models. Donations once targeted to a given service sector can always be diverted to intervening uses of which donors become aware (e.g. the new art museum). The pluralism-regional values framework would lead us to expect that the targeting of generosity would be consistent, i.e. places generous in their support of health and hospital facilities would also be generous in supporting educational and social services.

Competing federal generosity in the form of cash transfers to the needy or in-kind support for local services may completely or partially substitute for and crowd out local private or public efforts. The thesis examined in this study, however, suggests that federal substitution effects especially in the cash transfers have long since been absorbed. The relatively more generous places will make greater effort (within their means) to branch out and supplement federal efforts and compensate for federal retrenchment. The comparative analysis will need to test for these intervening opportunity and competing donor influences.

The Metropolitan Unit of Analysis

How can the comparative generosity of places be measured and what would be an appropriate local unit of analysis? The metropolitan level is an appropriate compromise unit for our study. States are too heterogeneous for a meaningful comparative analysis of community differences and the municipal level would be affected more by city-suburban factors than the regional pluralism which is the object of study here. The primary local health, educational, social and cultural institutions are supported through the taxes and contributions of residents from throughout the metropolitan area. American metropolitan areas differ considerably (although not, of course, as much as cities, suburbs, and exurbs) in their complements of welfare, education, health, and cultural services.

Metropolitan level analysis also makes sense because almost all private contributions are both raised and expended in the same communities or regions. Relatively little leaks outside to the rest of the nation or abroad. The metropolitan area is likely to be the primary marketplace for the solicitation of contributions, the optimun locale for purchasing corporate "good will," and for contributing to the service amenities employees can enjoy. The fortunes that established foundations were typically made in single metropolitan areas and are characteristically drawn to the support of local institutions. Individual contributions are used principally to support local institutions the donors themselves use and which they can observe others using.

COMPARATIVE ANALYSIS

The generosity of places can be examined in this study both through the direct charitable contributions of their residents to support services and the level and variety of local amenities requiring private and/or public subsidization. The objective in the empirical analysis is to examine the theses that: generosity differs significantly by region; local private and public generosity is consistent and movesin tandem; and place to place differences in generosity should persist after allowance is made for the effect of: resource factors (e.g. community size, homogeneity, stability, wealth, etc.); community needs or level of distress; the potential displacement effect of federal and state support for services; and the competing needs of cultural, health and educational institutions.

In functional form,

$G(s) = f(C,D,P,A)$

where: $G(S)$ = contributions targeted to social services (e.g. United Way and other umbrella groups)

C = economic capacity (indexed by population, employment, income, wealth, economic growth, etc.);

D = population distress (indexed by poverty levels, center city-suburban disparities, etc.);

P = public (federal, state, and municipal) support for local social services; and

A = alternative targeting of private donations (e.g. cultural, educational and health services)

Cash Contributions

Two alternative ways are used here to assess generosity across America's largest 85 metropolitan areas (those with more than half a million people). These areas differ significantly in affluence, and distress and in the level of federal, state, and municipal support targeted to local services. The poorest areas (as measured by median household income and population below the poverty threshold) are in the South or Rustbelt regions (including Birmingham, Greenville, Knoxville, Memphis, Scranton and Toledo) and the most affluent are the metro areas surrounding New York, but also San Francisco, San Jose, Washington, Minneapolis and Denver. Furthermore, the disparities are being intensified through differential job and income growth.

The first set of measures reflect direct contributions to local "umbrella" organizations represented here by the United Way, the Catholic Campaign for Human Development, and Jewish Federations. These contribu- tions cover only a portion of gifts, emphasizing support primarily for social and welfare services in the home community for 1986. United Way contributions are solicited in the workplace and tend, therefore, to be biased upward in favor of places with higher labor force rates and a higher percentage employed in large companies [Rose-Ackerman]. The data are clearly not a sufficient indicator of local generosity but become more revealing in examination of commonalty with Catholic and Jewish donations.

The United Way contributions whether examined on a per employee or per capita basis or relative to disposable income all show a ten fold difference between the most and the least generous metro areas. The Catholic Campaign for Human Development and the Jewish Federation fund drives for the same 1986 period show a seven fold and a twenty fold difference, respectively in the generosity extremes [Shields, etal.; Silberstein, etal.]. Furthermore, the United Way 1986 distribution over the 85 areas is entirely consistent with the 1972 pattern (r = .73) and the Jewish Federation 1986 giving is consistent with 1981 (r = .90). The patterns are not only separately stable over time but consistent with one another across the metropolitan areas (r = .45). Not surprisingly, United Way giving is in tandem with Catholic and Jewish generosity.

The Effects of Resource Capacity

Are contributions highest in the most affluent or the most distressed communities, where federal expenditures are highest or lowest, and where the competition of other service sectors is greatest or least? The regression equation includes variables which index each of the four factors [capacity, distress, public generosity, and philanthropy alternatives] presumed to account for the variations in United Way giving across the 85 areas. The regression analyses show higher giving rates in the moderate income and less distressed communities with more of a manufacturing than service economy and declining rather than growing in jobs and income. Giving is higher in the more accessible than more remote metropolitan areas and where there are fewer aged people and members of minorities. Metro areas with much higher giving rates than expected on the basis of resources and size are Cleveland, Detroit, and Rochester; those with much lower than expected rates were Los Angeles, Salt Lake City, and the Florida metro areas.

The effects of distress levels

Theory suggests somewhat greater generosity in the presence of need or distress but the United Way, Jewish Federation, and Catholic donations generally show the opposite effect. Higher poverty, crime, and minority population are reflected in lower rates of giving after allowing for the effects of population size, median income, and public sector funding support [see Carson]. The only distress variables directly related to giving levels are such measures of heterogeneity as center-city/suburban income disparities and the "proportion of children born to women younger than 20." A reasonable interpretation of these findings is that donors tend to be more generous when they can assume the recipients of services will be much like themselves, an assumption difficult to maintain in a metro area with strong cultural, social, and racial differences. Metropolitan areas with much higher giving rates than expected on the basis of distress levels are Cleveland, Detroit, Seattle, and Minneapolis and much lower than expected rates occurred in Los Angeles and the New Jersey suburbs of New York City as well as Grand Rapids and Phoenix.

The effects of public generosity

Private contributions should theoretically be displaced or "crowded-out" by public expenditures that provide true substitute support for community and social services. The contributions should be relatively low in those metro areas that are recipients of generous public funding from federal, state, and local sources. Private donations should be higher in those communities receiving little public funding. As noted earlier, however, displacement interdependencies are complex because complete substitution would be relatively rare. The most likely prospect of crowd-out would be in the relation of federal to state expenditures. Since local private and public generosity are expected to be consistent and applied to different uses than federal transfers and grants, we should not expect to find federal crowd-out or joint crowd-out of local efforts. Area differences should be reflected in the degrees of local effort and displacement.

The analyses (holding the other factors constant) show a modest negative (i.e. crowd-out) effect of federal expenditures on private contribution levels but a positive relationship between donations and state and especially municipal assistance. Local public generosity appears to move in tandem with private contributions. On the other hand, the variable indexing state and municipal supplements to AFDC payments is related directly to numbers of residents on AFDC and minority and aged population and inversely to local private generosity. Private and local public support of amenities is more prevalent in the less populous and moderate income areas, while income transfers are more generous (predominantly by state government) in bigger metropolitan areas with larger low income minorities. These findings are in general agreement with other analyses of the joint crowd-out of charitable and local public financing of services by federal programs [see Steinberg]. Rochester, Hartford, Cleveland and Cincinnati show much higher contributions and the New Jersey and Florida metro areas and Phoenix show much lower rates than would be expected from the local public sector assistance and transfers.

The effects of alternative targets for generosity

If one assumes that donors contribute a fixed proportion of income each year, then potential recipients must compete for their share. The opposing view is that since such a small share of disposable income is donated (i.e. about 2%), donors can easily augment their contributions if "properly solicited" without reducing their level of consumption or quality of life.

Do the metro areas differ in availability and access to amenity services? Unlike basic and public services, the amenity services typically require some partial subsidy support to be made available to all who could benefit. The variables index the variety, magnitude, and quality of services in the educational, cultural and health sectors. The education index, for example, combines: university ratings, college attendance, pupil-teacher ratios in elementary school and expenditures per high school student. The health measure indexes: health care costs, doctors per capita, specialized hospital departments, and area air pollution and flouridation. The arts index includes libraries, museums, symphonies, theatres, opera and dance companies. The index measures the number of facilties, budgets, number of performances, etc.

The education scores are especially high in New England metro areas, but also in Rochester, Albany, Washington and Raleigh-Durham. The scores are lowest in Sunbelt and Rustbelt places. The health index is best in some of the largest cities and relatively weakest in the smaller Rustbelt places. The cultural amenities are strongest, of course, in the largest centers of New York, Los Angeles, San Fransisco, Philadelphia, and Boston.

In general, one must conclude from the measures that amenity differences even between metro areas of more than half a million people are quite significant. Some of the places have access to a wide variety of high quality services in all three sectors, while others rank low consistently or have quite mixed scores. The measures are gross but they point to persistence of regional differences not only in access to services but in the public and private generosity that supports their provision. Residents of Boston and Minneapolis at one extreme are much better served than those of San Antonio and Birmingham.

The analysis of United Way contributions shows them to be consistent by area with support for cultural and health and hospital institutions and inversely related to support for educational facilities. Umbrella group contributions are much higher than expected from the support for arts, educational, and health organizations in Cleveland and Cincinnati and much lower than expected in Los Angeles and Salt Lake City. One might expect to find a higher level of service amenities in larger cities because of the threshold population numbers needed to fill concert halls and to listen to public radio. Agglomeration economies would also help to explain why ballet, opera, and university ratings should coincide by area.

Is support for educational, health and cultural services simply a function of population size and community wealth? The analyses test the effect on service levels of metro area population, median income and a variable measuring locational centrality or accessibility. The findings tend to confirm our expectations: population numbers are most important to cultural and health services; educational amenities are affected more by income levels; and the access measure is important in all three sectors (suggesting that these services are likely to have regional use extending beyond single metro areas. The addition of the variables indexing distress and poverty levels confirm their expected negative but not significant influence on service access. Health, educational and cultural services are not well targeted to the poorer metro areas.

SUMMARY

Will greater decentralization (from the federal government to states and localities) of responsibility for supporting cultural, health, educational and social services result in wide regional disparities in well-being and quality of life? The study examines the diversity of generosity patterns in America's states and largest metropolitan areas. The findings indicate: that generosity levels differ significantly between the areas; that local private and public generosity is consistent rather than competitive but is expressed more in civic improvement and support for amenities and services than in charitable transfers; and that support for social services is also consistent rather than competitive with support for local cultural and health (but not educational) institutions. Generosity levels are higher in moderate income communities without much distress and with a relatively smaller proportion of minority and aged residents.

Some of the generous communities and/or their states also provide substantial income and service supplements to their AFDC residents; while other communities provide neither generous local amenities nor significant supplementary aid to their dependent populations. Communities whose states are generous to low income residents generally provide more meager private contributions. A complex set of place variables at local and state levels, therefore, produces different kinds of environments for public and private support of different kinds of service activities. Decentralization could be effective in some places but would likely be hazardous in others without an ample safety net.

NOTES

[1] Space does not permit inclusion of regression analysis tables. Copies may be obtained by writing to Julian Wolpert, Woodrow Wilson School, Princeton University, Princeton, N.J. 08544.

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HISPANICS AND PHILANTHROPY:
POLICY ISSUES TO THE YEAR 2000

by

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Prepared for the 1988 Spring Research Forum
"Looking Forward to the Year 2000:
Public Policy and Philanthropy"

San Francisco, California
March 17-18, 1988

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HISPANICS AND PHILANTHROPY:
POLICY ISSUES TO THE YEAR 2000

On January 1, 1988, the Washington Post declared that Hispanics are "IN" in 1988. Although I am not certain what that means, I do know that Latinos are certainly receiving much more attention lately. Major policy analyses have been published by the Carnegie Forum for Education and the Economy, the National Alliance of Business, the National Governor's Association, the National Educational Association, and the Committee for Economic Development, just to name a few, citing the national importance of addressing the needs of Hispanics and other minorities. These reports state that if America does not effectively train the growing minority population, national competitiveness will be negatively affected. They note that the increasing proportion of Hispanics and other minorities in the work force compels the nation's educational system to ensure that these future workers have the skills America needs to compete favorably in the world.

Being "in" or fashionable has paradoxical consequences for Latinos. Organizations want to discuss minority, "at-risk", disadvantaged, and Hispanic populations. Many wish to develop policies to address Latino needs. However, most often Hispanic representation in policy making bodies is nonexistent, and participation is token. Mainstream non-profit organizations, foundations, and corporations have few or no Hispanics on their governing bodies, or among their senior staff, and more often than not, non-Hispanics define Hispanic needs, develop solutions, and implement the programs.

A number of Latino organizations have also undertaken policy research studies and evaluating solutions to social problems that Latinos face in this country. The purpose of these efforts have been to impact public policy. However, limited access to resources often restricts the potential affect of such studies which are especially important because they represent Hispanics' views of their own needs.

The ASPIRA Institute for Policy Research has recently completed a report on the needs of Hispanics in the Northeast in which recommendations are presented for the public sector, the private sector and for Latino communities themselves.[1] A major purpose of the study was to assist the philanthropic community in identifying and seeking solutions to the problems faced by Latinos in the Northeast and to provide a guide for action. This paper will focus on one part of our findings, that of the role that the philanthropic sector in addressing Hispanic needs.

FINDINGS

The report Northeast Hispanic Needs: A Guide for Action is based on the results of an invitational conference and a survey of over 400 Latino leaders in five states (Connecticut, Massachusetts, New Jersey, New York, and Rhode Island).[2] Latino population in these states is estimated at 2.7 million and is concentrated in large urban areas. Leaders were identified through our database of elected and appointed officials and directors of community organizations, and by reputation or recognition by other Hispanics.

Study participants listed over 80 needs of Latino communities in the Northeast in areas encompassing education and training, political education and empowerment, health, housing, human services and community economic development. The following are the top ten needs identified:

1. Increase Hispanic school attendance and reduce dropout rates.
2. Increase quality housing for low-income Hispanics.
3. Increase the number of Hispanic voters.
4. Increase the representation of Hispanics in elected and appointed offices.
5. Increase Hispanic representation in administrative and policy-making positions at all levels of the educational system.
6. Promote the development of Hispanic leadership.
7. Increase the availability of training and support programs to facilitate the entry of Hispanic women, youth, and unemployed persons into the work force.
8. Improve the delivery of health care in the Hispanic community for all age groups, from prenatal care to gerontology.
9. Increase the Hispanic community's understanding of the political process at the national, state, and local levels.
10. Increase Hispanic representation on housing policy-making bodies; i.e., planning, zoning, and housing boards.

All the approximately 80 needs identified were connected by three common themes: representation, responsiveness, and empowerment.

Representation needs include increasing Latino access to resources, leadership positions, employment, and training opportunities. While expressing a desire for greater levels of representation in the political process and in policy-making bodies, Hispanic leaders also indicated a need to reduce overrepresentation among school dropouts, the poor, the unemployed, substance abusers, pregnant teenagers, and AIDS victims.

The second category, responsiveness, comprises needs for improving and expanding delivery of social and educational services, effectively combatting discrimination, and increasing public awareness of and sensitivity to Hispanic concerns. In short, Latino leaders expressed the opinion that the external social conditions that affect Hispanics should be improved and that the public and private sectors should be more responsive to Hispanic needs.

A third set of needs deals with issues of empowerment. With the conviction that knowledge is power, Hispanic leaders indicated that their communities frequently lack information and skills to make decisions such as those concerning their participation in the electoral process or those necessary to secure good jobs. The empowerment category encompasses needs related to the internal conditions of Latinos and their communities, such as developing the leadership skills of Latinos and increasing the involvement of the community in the solution of its own problems.

The leaders who participated in the study recognized that the complex nature and wide range of problems confronting Latinos do not lend themselves to simple solutions. There are no quick answers, no ten easy steps for improvement. However, six key principles were identified that can serve as guides for philanthropy to promote the social and economic advancement of Hispanics in the United States.

PRINCIPLE ONE: FOCUS ON STRENGTHENING SELF-HELP

The Hispanic communities have many effective organizations and programs and skilled individuals. New initiatives should tap these talents, build on these strengths and endeavor to transform the traditional welfare approach to one of skill building and employment generation.

Participants suggested that funders should recognize that Hispanic community-based organizations provide highly effective complementary services to schools and social service agencies--services that other non-Latino organizations generally are unable to offer. Latino agencies play a vital role in the Hispanic community.

Hispanic leaders recommend that funders support the efforts of Hispanic community-based organizations by:

1. Contributing general operating funds to strengthen their infrastructure. Community-based organizations need to develop their infrastructures to assure stability. This requires general support funds, but most funding institutions prefer to fund defined projects. While project overhead provides some unrestricted funds, it is too piecemeal and inadequate to promote sustained organizational development activities;

2. Supporting activities that would improve the ability of community-based organizations to raise funds, such as documenting the effectiveness of their programs or increasing membership;

3. Providing both funding and technical assistance personnel for activities that will strengthen the organizations' infrastructures and improve the professionalism of their staffs, especially in such areas as budgeting, strategic planning, fund raising, and proposal writing;

4. Ensuring continuation of non-program activities, such as public relations, which are essential for public recognition of the organization's activities and which, in turn, make the organization more attractive to funding sources;

5. Assisting with cash-flow problems. There often are funding gaps between the end of a project year and the award letter from a government agency which require organizations to reduce staff and cease all work on a project or go into debt;

6. Providing technical assistance through mechanisms such as executives-on-loan;

7. Making in-kind contributions of equipment and supplies; and

8. Making surplus space available to community organizations.

PRINCIPLE TWO: EMPHASIZE PREVENTION

Investing in the development of the young has been shown to avoid costly interventions later on. Children derive great benefits from an early start. Programs that motivate and build the self-confidence of Latino youth, and programs that ensure adequate health and housing should be supported. Latino leaders recommend the philanthropic community to:

1. Increase support for programs proven effective for Latinos, especially the youth;

2. Help create a greater awareness of the increasing impact of Hispanics as consumers and workers;

3. Establish funding of Hispanic initiatives as a priority area;

4. Finance the development of creative, culturally relevant day-care programs at employment sites and in local communities;

5. Fund training for Hispanic workers, especially women, who are currently offering informal and formal child care so they are better able to care for Hispanic children;

6. Assist in the development of literature and other information sources to assist in evaluating child-care services; and

7. Provide incentives to employees to work as volunteers and mentors for Latino youth.

PRINCIPLE THREE: STRENGTHEN LATINO LEADERSHIP

Greater Hispanic representation at all levels of decision making will promote greater responsiveness to Latino needs. Youth should be encouraged and supported in developing their leadership potential. Participants recommend that efforts be made to:

1. Increase the number of Hispanic administrators on policy-making and resource allocation bodies within philanthropic organizations;

2. Support organizations that promote community awareness of the importance of participating

in the political process and those that promote voter registration;

3. Collaborate with community organizations in creating leadership development programs, including internship and mentoring opportunities for Latino adults and youth. Participants agreed that planning for leadership succession and continuity is vital. Staff training and leadership development programs for middle-level managers and other employees of community agencies could help ensure the availability of new leaders in community organizations; and

4. Create support networks and mentoring opportunities within mainstream organizations to assist in the professional growth of Hispanic employees.

PRINCIPLE FOUR: PROMOTE INFORMATION EXCHANGE

Disseminating information on successful programs and experiences and on local, regional, and national data on Hispanics stimulates discussion of similarities and differences and encourages better planning to meet Latino needs. Convening Latinos on a regular basis is essential for developing active networks and encouraging articulation and coordination. Leaders indicate that the philanthropic community should:

1. Support efforts to convene Latinos on a regular basis for information exchange and planning;

2. Disseminate information on corporate and foundation donation patterns to Hispanic organizations;

3. Help identify and publicize successful program models that exist in the Hispanic community and models that can be replicated by Latino organizations;

4. Disseminate information regarding opportunities for Latinos to provide services and products to large corporations;

5. Finance hotlines that will offer bilingual information to Hispanics about emergency services and programs in health, housing, and human services; and

6. Support research, policy analysis and dissemination from the perspective of culturally and linguistically diverse groups.

PRINCIPLE FIVE: BE HOLISTIC AND COMPREHENSIVE

When dealing with individuals, effective policies and practices should focus on their broad range of needs. Just as the educational achievement of children cannot ignore their health and living conditions, improving the condition of Latinos must not be viewed as dependent on the solution of one isolated set of problems. The inherent interrelationship of Latino needs requires comprehensive and integrated efforts. Latino leaders urge the philanthropic community to:

1. Support programs that address a broad range of Hispanic needs;
2. Promote links between programs serving the needs of Latinos to encourage comprehensive approaches; and
3. Broaden employee benefit programs to include family health care and day care plans.

PRINCIPLE SIX: ENCOURAGE COLLABORATION

Hispanic organizations, federal, state, and local governments, private employers, and universities should join in the effort to address Latino needs. Building on the strengths of Hispanic communities, a combination of public and private efforts and resources must tackle the task of addressing emerging and lingering needs of the Latino communities. Participants advise philanthropic organizations to:

1. Provide incentives for their own personnel with skills in such areas as budgeting, strategic planning, and fund raising to serve on the boards of directors and advisory boards of community-based organizations;
2. Ensure that resources allocated to traditional non-Hispanic organizations are providing services to Hispanics in proportion to their representation in the local population;
3. Play a major role in convening community-based groups to develop community-wide plans and strategies. This kind of meeting should take place in a retreat setting, away from the day-to-day pressures of the office. Sufficient time is required to delve into the issues in depth and to develop workable strategies;

4. Develop programs to provide small Hispanic businesses with access to training in financial management techniques and credit consultation and advisement;

5. Provide challenge grants for projects that involve collaboration between community organizations, private enterprises, and local, state or national government agencies;

6. Seek the counsel of Latino leaders and community spokespersons on how to collaborate in the solution of problems facing the local communities and the nation; and

7. Develop awareness of the benefits of collaborating with government agencies and community organizations to promote the social, economic, and educational advancement of Latinos. Participants indicated that funding sources should assist Latino communities not only out of a sense of responsibility, but also because it is in their best interest to help ensure the progress of tomorrow's workers and consumers. The Hispanic market is growing in importance and its buying power is increasing, yet problems such as the high drop-out rate are taxing corporate dollars. Moreover, many of the needs of Latinos--although often more aggravated--are shared by the entire population.

Latino leaders are very much aware of the need for a meaningful Hispanic presence in public policy making, in the absence of which, new programs are not very likely to have the desired outcomes.

Hispanic leaders conclude that there are no quick and easy solutions to the problems faced by Hispanics. Their recommendations outlined in this paper present key features of effective programs and action strategies. But to remain responsive to emerging needs, local groups must continue to be a major force in efforts to address Latinos' most pressing problems. Harnessing community energy, forming working partnerships, mobilizing talent and resources require a sustained and concerted effort on the part of community organizations, the independent sector, and local, state, and federal governments. The needs are great, and so must be the joint effort to address them.

ENDNOTES

1. ASPIRA was founded in 1961 in New York City to address the alarming drop-out rate of Hispanic students and promote leadership development among Latino youth. It currently has offices in New York, New Jersey, Pennsylvania, Illinois, Florida, and Puerto Rico, and the national office in Washington, DC. ASPIRA programs assist over 14,000 students annually.

   In 1985, the ASPIRA Institute for Policy Research was founded to expand the research and policy analysis capability of the ASPIRA Association. The objectives of the Institute are to:

   - undertake policy analysis and research focusing on the urgent needs and problems confronting the Hispanic community at national, state, and local levels;
   - prepare reliable and timely reports that assess and interpret prevailing policies of special concern to Latinos, providing alternative approaches and challenging commonly held assumptions;
   - collaborate with public and private organizations in joint projects related to the education of Hispanics;
   - develop pilot projects that address major educational needs of Hispanic students, as determined by needs assessments and data analyses, to serve as model programs for local, state, and national decision makers;
   - increase the number of professional Latinos in educational policy analysis and research by serving as a research center for experienced researchers and interns; and
   - advocate in favor of Latino youth and the Hispanic community by coordinating, preparing, and presenting policy analyses to appropriate decision-making bodies.

2. This paper summarizes part of the findings of the report, Northeast Hispanic Needs: A Guide for Action. Copies of the two-volume report are available for $18.50 plus $1.50 shipping charges from the ASPIRA Association National Office, 1112 16th Street, NW, Suite 340, Washington, DC 20036.

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SECTION TEN

PUBLIC POLICY AMONG MAJOR SUBSECTORS

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THE DELEGITIMATION OF THE NONPROFIT SECTOR: THE ROLE OF IDEOLOGY AND PUBLIC POLICY

by

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The 1980s have proven a time of crisis, turmoil, and change for the nonprofit sector, both in terms of the day to day operation of nonprofit organizations and in terms of larger issues concerning the role of the sector in relation to other sectors of society, namely, government, business and the public (citizens). These changes reflect shifts in public policy as well as in public perceptions concerning the role of government and the nonprofit sector (NPS) with regard to the provision of certain services.

This paper examines the legitimacy of the NPS as a viable and significant entity in the context of its place as a distinctive "third sector" of the economy and polity. Legitimation, and its opposite, delegitimation, are deceptively simple concepts, but ones that are crucial in denoting the strength and viability of any society and its social institutions. Legitimacy refers to the degree to which social systems or institutions are valued (Weber, 1958) and their underlying principles and legal authority accepted by members of society (Scharr, 1984). A stable NPS depends not only on its economic and organizational viability, but also on its ability to generate and maintain support in the political system for its right to exist as a legitimate sector of society. Just as the legitimacy of the government depends upon the effective performance of its functions, at least as defined by the most powerful groups in society, and preservation of the existing social order, the legitimacy of the NPS depends on the assessment by powerful forces, institutions and sectors in society of its performance.

When the underlying beliefs, laws or principles that support societies or institutions are questioned or challenged, their basic legitimacy is questioned or challenged. Such legitimacy challenges, by definition, generate power struggles of enormous economic, political and ieological moment. The processes of legitimation and delegitimation, are the attempts, respectively, to bolster or undermine support for existing authority and modes of organization. Given that every social order, institution and organizational entity requires legitimacy to exist and persist, powerful and successful legitimacy challenges, i.e., the actual delegitimatation of such major institutions as government or the NPS, are extremely serious. Legitimacy challenges generate crisis tendencies (Habermas, 1975) and provoke periods of intense uncertainty as preexisting understandings are called into question and "new power centers confront existing [power] structures" (O'Connor, 1987, p 145). A full-blown legitimation crisis occurs when there is a resulting breakdown in the supporting norms and institutional rationale for a sector such as the NPS, because its organization and activities can proceed only insofar as there is legitimacy available.

Consistent with recent thinking on the interpenetration of the NPS with govenrnment and business in the larger political economy (Van Til, 1982; 1987; Ostrander, Langton and Van Til, 1987), legitimacy issues surrounding the NPS cannot be understood apart from considerations of the roles and problems of government and the business sector. In the long term, research on legitimacy of the NPS must fully specify the relationships between the state of the economy and the issues faced by business, the legitimacy questions facing government, and problems confronting the NPS.

The sources of legitimacy of the NPS reside in its historical and contemporary role and character. An important ideological aspect of the NPS, about which much has been written, has been the notion that it is an independent sector - one that stands between (and protects) society from a vast ignominious bureaucratic and stifling government. The dilemma of this view of an independent NPS is that, while it has supported the notion that the NPS is a positive force against an overly-powerful government (anti-state), it has also supported the notion that the NPS does not need government, or is somehow unrelated to it. This has left the NPS vulnerable to attacks on its base of support both in law and in government funding (Hall, 1987; Salamon, 1987).

In addition to serving as an alternative provider to government, NPS institutions in U.S. society have enjoyed special legitimacy in terms of their traditional representation of pluralistic, participatory and non-economic motivations of: charity and the spirit of giving, privatism, individualism, and the democratic impulse. Legitimacy questions inhere in the necessity for the NPS to straddle these values and the newly imposed efficiency criteria in the context of an increasingly austere and competitive environment.

Recently, the situation of the nonprofit sector has been typified in terms of crisis and crisis tendencies (Hall, 1987; Estes and Alford, 1987). Hall (1987) contends that three types of crises have occurred: (1) a crisis OF the NPS, comprised of the shifting role of government vis a vis society and the NPS within it; (2) a crisis WITHIN the NPS, comprised of problems of insufficient professionalism and managerialism; and (3) a crisis in "nonprofit scholarship". This paper considers the legitimacy issues raised relative to the first two types of crisis and to our own research on crisis tendencies and the NPS.

The crisis OF the NPS consists of a number of dimensions: government cutbacks and defunding; federal and state challenges to nonprofit organizational status including legal, tax and regulatory changes that affect the organization, management, revenues (e.g., treatment of related income; incentives for individual and corporate giving), and activities permitted by nonprofit organizations, such as advocacy limitations (Skloot, 1987; Broaddus, 1987; Estes, Alford and Binney, 1987).

The crisis WITHIN the NPS consists of pressures to embrace professionalism and managerialism, which emerged as early as the 1969 Tax Reform Act (Hall, 1987) but which have been accentuated in the current climate of competition, and the restructuring of community services that has resulted from a combination of external and internal pressures on the state and the NPS in the present era of austerity (Estes and Wood, 1986; Estes and Bergthold, 1988; Estes, Alford and Binney, 1987). Our research has identified multiple dimensions of this restructuring at the community agency level, for example, in the provision of home health there are: organizational and labor force changes (increasing part-time and contract personnel); client and service changes based on ability to pay; a shifting ideological rationale for nonprofits, threatening goal-displacement (a "means-ends" inversion in which the "process goals" of management and survival replace the "end goals" of service, charity, and democratic participation); and, in a limited number of cases, organizational death.

For purposes of this analysis, the concepts of legitimation-delegitimation must be disaggregated into conceptually and empirically measurable components. Friedrichs (1980) argues that legitimacy crisis may be expressed in terms of three dimensions: (1) subjective or perceptual, including ideological and attitudinal changes and challenges; (2) objective or behavioral, including actions taken by individuals, policymakers, groups, and others; and (3) a structural dimension based on the characteristics of the state, economy, and society.

All three dimensions are relevant, but the first two can be employed at two levels of analysis, "macro" and "micro", to signify the different levels at which legitimacy challenges can be observed (See Figure I). Macro-level perceptual and behavioral indicators of legitimation problems evince themselves in the broad institutional relations and transactions between different sectors of society. Micro level indicators reflect those changes occurring at the level of the individual nonprofit organization or subsector of nonprofits, such as health or social service agencies.

On the macro-level, there are a series of perceptual indicators of legitimacy problems for the NPS in relation to other sectors of society. A number of these reflect struggles for the ideological center-ground in the American value structure. The foresight of John Gardner and the founding of INDEPENDENT SECTOR (IS) in 1980 is an early manifestation of the acknowledgement of troubles on the horizon for the NPS. The efforts of IS to claim (reclaim?) the inherently social values of giving, volunteering and the not-for-profit initiative in the context of the most conservative and politically organized anti-state hostility in recent memory is no coincidence.

Talk of crisis (from the family to the economy), the politics of austerity, the profitability problems of business, and the attack on government (ie., on its legitimacy) each signalled potential storm clouds for the NPS. Simultaneously a wave of books appeared on crisis at the societal level, including Legitimation Crisis (Habermas, 1975) and The Limits of Legitimacy (Wolfe, 1977), while public opinion pollsters averred that there was a "crisis of moral leadership" and "resentiment in America" (Yankelovich, 1972; 1975; Caddell, 1979), and social scientists worried about Watergate and other problems. "Serious enquiries into [the] future" of the NPS emerged in the 1970s (Hall, 1987, p 20), resulting in the privately sponsored Filer Commission resport (1975) and the Department of Treasury's seven volume publication on the Commission and the NPS in 1977. Articles and books on the NPS appeared on "The Changing Position of Philanthropy in the American Economy" (Dickinson, 1970), "Federal Oversight of Private Philanthropy" (Ginsberg, Marks and Wertheim, 1977) and The Endangered Sector (Nielsen, 1979), as balancing the preservation of sectoral independence with increased public accountability and government funding claimed center-stage of nonprofit concerns from the mid-1960s to the late 1970's.

For the 1980's, an opening salvo in the ideological struggle over NPS legitimacy was delivered in the Small Business Administration's (SBA) report, "Unfair Competition" (U.S. SBA, 1984), assailing nonprofits as unfair to small business and calling for eradication of tax treatment differences between nonprofits and for-profits. Fallout from this report continues to be felt in the form of various policy remedies now being pressed in several states (Skloot, 1987).

Additional indications of ideological battle-lines drawn between norms of the market, competition, and efficiency versus those of charitable service and non-economic motivations are found in the 1987 U.S. House hearings of the Ways and Means Oversight subCommmittee and proposals to tighten federal tax advantages for nonprofit hospitals and other health nonprofits (Health Policy Week, 1987). The recent counterattack of the nations's oldest federated charity, the United Hospital Fund of New York City, is another example (Seay and Vladeck, 1987). The Fund's response has been to develop a campaign under the banner, "Mission Matters", which:

> grew from a need to inform, and to balance what has evolved into a skewed public policy debate about the legitimacy of the not-for-profit organiazational form as a result of a preoccupation with entrepreneurialism and competition, rather than social responsibility in health care (Vladeck 1987).

This document highlights the distinctive character of nonprofit hospitals: their commitment to social values, to the community, and to their patients and services regardless of profit orientation; their governance and accountability to maintain a charitable organizational basis; and their institutional volunteerism. The Fund's "fight back" strategy is defining the domain and staking the claim to the culture of caring by documenting the norms and traditions of service of nonprofit hospitals, institutions that "conduct more medical research and provide more education and community health care services" than do for-profits ($22 billion in charity care in the past five years).

On the behavioral/objective macro-level, there are two dimensions of import: political and economic. Evidence of macro-level political struggles with significant economic ramifications are the 1982 and 1986 tax reform bills, both of which contained tax provisions that, it was argued, would have a profound (and constraining) effect on economic incentives to give privately to nonprofits. The 1982 Tax Equity and Fiscal Responsibility Act reduced taxes by $750 billion, theoretically providing more opportunity for charitable giving; however, its substantial depreciation allowances and tax write-offs actually reduced incentives for corporate and individual giving. The 1986 Tax Reform Act abolished the charitable deduction for individuals that do not itemize their income taxes, a move that was anticipated to be a "blow" to individual giving incentives (Clotfelder, 1985; Simon, 1987).

Political problems for the NPS also surfaced in: (1) the legal challenges to the favored tax treatment of nonprofits in terms of related income; (2) regulatory changes requiring nonprofits to incorporate the equivalent of for-profit taxes in bidding for government contracts (to make them less "unfair" to for-profit bidders) (Skloot, 1987); (3) federal regulations restraining advocacy activities by nonprofits (Broaddus, 1987); (4) regulatory provisions encouraging competition and the entry of proprietaries in the health field (Marmor, Schlesinger, and Smithey, 1987); and (5) multiple pressures for increased organizational rationality (i.e., efficiency) of nonprofits.

Behavioral/objective macro-level economic challenges appear largely in the form of budget cuts and defunding that have dramatically affected the NPS. Documentation reveals total cuts of 28% in federal support for nonprofits between 1980 and 1986, excluding health finance (Abramson and Salamon, 1986, 73). Additional, and significant cuts are projected in federal support of nonprofit organizations (exceeding $22 billion) for the FY 1987 to 1989 period based on budget proposals, bringing overall federal reductions to more than 40% per year below 1980 funding levels (Abramson and Salamon, 1986, xvi). At the same time major health cost containment policies have been introduced. With the economic stringency placed particularly on social services, community development, the arts, education, and health services (exclusive of health financing) in the 1980s (Salamon and Abramson, 1982; 1985), the viability and survival needs of NPS organizations are key issues. These struggles have brought the legitimacy claims of the NPS into even sharper focus as of the late 1980s.

To this point, evidence of the effects of the tendencies toward legitimation crisis faced by government and its subsequent effects on the NPS, has not been systematically documented. The following data from our current research on the impact of federal cost-containment policy on the delivery of health and social services for the elderly offer some of the only available data, albeit preliminary, on behavioral and perceptual/attitudinal indicators of the changing roles of nonprofit, for-profit, and public service sectors, as well as the perceptions of community service agencies about the legitimacy of guaranteeing protection advantages (via 501c3 status, tax advantage, advantage in competitive bidding, etc.) to any one of these sectors over the others. Preliminary data analysis indicates widespread environmental turbulence and uncertainty in the home health provider community, with all three sectors experiencing change. Also what is apparent is that behavioral indicators of role change often exist in contradiction to perceptual and attitudinal beliefs about what each sector's "proper" role is, and the degree to which it is appropriate for the state to support or favor, as has traditionally been the case, one sector over another.

Following our model, the data presented are micro-level indicators drawn from a study of a number effects of federal health policy changes since 1983 which have contributed to restructuring of the nonprofit health and social service sector. Interviews in 1987 with a random sample of nonprofit and proprietary home health agencies in nine urban communities (SMSAs) in five states document both the behavioral and ideological dimensions of the legitimacy struggles being waged on a day to day basis by nonprofit health and social services organizations. 193 home health agencies in the study sample were asked to assess the changes in the role of nonprofit, forprofit, and public agencies in the delivery of health and social services to the elderly over the past three years.

On the micro-behavioral level, a substantial majority of all respondents reported that all three sectors had undergone changes in their role, with approximately three-quarters describing changed roles for both the nonprofit and proprietary for-profit sectors and two-thirds for the public sector (See TABLE I). Preliminary analysis of survey questions about the nature of the change in these sectors yield interesting and provocative results. In describing the nature of changes in the NPS, almost half (48%) of the responses indicated an increased NPS role and another one-third (33.5%) reported that its role had decreased in the provision of health and social services for the elderly (See TABLE II).

The most frequently cited reasons for an increased NPS role include:

- the increase in the demand for services and/or the demand for an expanded scope of services;
- increases in client pressures (including a dramatic increase in the need and/or expectation of the NPS to care for indigents and those unable to pay);and
- changes in client patterns (including an increase in numbers of clients and an increase in the number of sicker clients).

Two primary reasons were cited for the decreasing role of the NPS:

- an inability or unwillingness of sector agencies to provide services; and
- specific financial reasons including a decreased role due to reimbursement changes, increased fiscal constraint, and overall decrease in the assumption of responsibility by the NPS.

In general, those claiming a decreased role for the NPS cited economic reasons (decreased funding, inability to provide services due to lack of funding, tightening eligibility due to reimbursement, etc.). On the other hand, those who cited an increased role for the nonprofit sector predominantly cited reasons of demand and "need". This apparently contradictory set of responses - the simultaneous "push" and "pull" on the NPS - illustrates that changes in the NPS role are clearly tied to fundamental changes in the macro-level financing structures of health and social services, and agencies are currently facing a crisis of increased demand concurrent with decreasing resources in a competitive and increasingly privatized environment of health care delivery (Estes and Wood, 1986; Bergthold, Estes, Alford and Villanueva, 1987).

Interestingly, a majority of respondents cited a similar change in role for the public sector, with reasons supporting both the case of an increased and a decreased role very much like those of the NPS. Thus our data indicate that, like the NPS, the public sector is facing a situation of increased magnitude and scope of need and demand and an environment of high fiscal constraint. However, given the current dominant ideology which discourages the public provision of services and encourages privatization of welfare state activities, the NPS faces a different dilemma from the public sector. While public sector provision of such services has been attacked under the guise of cost-containment, there is still considerable support for some system of public provision at the level of last resort (and to prevent the forprofit sector from directly having to absorb the costs of those who cannot pay).

Attacks on the traditional mission of the NPS and its right to tax advantages and other forms of state protection and the pressures of survival in a highly competitive and cost-containment conscious environment, pose a considerably different dilemma for the public sector. To understand the significance of this dilemma and the effects of attempts to delegitimate the NPS, the data on NPS must be contrasted with those on the proprietary sector.

The responses regarding the role of the proprietary sector differed in important ways from those on the NP and public sectors. The primary for profit change was toward an increased role (51.1%), while only 17.8% of the responses cited a generally decreased role for this sector. The increased role of for profits was largely attributed to similar factors cited for the other two sectors: service-oriented responses, including increased demand, a more diversified/expanded scope of services, more home care and skilled home care, and more high-tech care. However, for profits were more likely to report targeting full-pay patients, a response that did not appear in responses about the other two sectors, and virtually no response indicated increases in indigent or partial-pay care in explaining the for-profit sector's increased role.

While funding considerations were a major factor in the declining role of NPS agencies, in the case of for profits, only a small percentage of the responses cited funding considerations. The most important reasons for a diminished role for proprietaries are:

- a narrowing scope of services;
- the ability to provide only profitable services;
- a tendency to decrease or drop Medicare entirely; and
- a "turning away from the elderly"

Issues of competition, marketing and public relations are all strongly tied into the interrelationship and changing role of the various sectors. In general, the changing role of the three sectors can be differentiated on the basis of two factors: response to fiscal condition and response to demand. Overall, a dramatic increase in demand has been documented. But from our data, the nonprofit and proprietary sectors have responded differently to this demand. Our informants have described the successful targeting and efficiency practices of the proprietary sector, strategies adopted in order to maintain solvency and profitability in a competitive environment. But pressures toward practices supporting efficiency, solvency and "profitability" cited by informants in describing the NPS, it is clear that that sector is being forced to adopt the practices of the proprietary sector - practices that may threaten not only the traditional role of the NPS, but also its ability to meet the increased demands being placed upon it, particularly in the provision of care to indigent and partial-pay clients. Further and most important, such behavior by nonprofits is likely to contribute to the delegimation of the NPS.

One of the aforementioned bases of attack on the NPS has been the perception that, despite enjoying tax exempt status and other advantages, nonprofits have begun acting like proprietaries. A second basis upon which the attacks are based is the relative efficiency of the sectors in providing for community need, especially in the current environment rife with cost-containment rhetoric. However, our data indicate that while the NPS is being forced to meet proprietary standards of efficiency (efficiency measured in terms of costs, but not in terms of quality or access), NPS agencies are simultaneously being asked to meet the increased demand caused in part by the federal Medicare cost-containment policies and by the ever-increasing ranks of the un- and underinsured (which, by definition, will make nonprofit agencies "inefficient").

These micro-level behavioral indicators are of particular interest in light of data on attitudinal indicators of the delegitimation of the NPS. Agencies in our study were asked whether public policy should favor or protect any one of the sectors over another. The responses provided much insight into the ideological contradictions in the role of the NPS with respect to the other sectors, government and business.

The dominant perceptual and ideological view of study respondents is that the NPS should not receive special treatment (e.g., tax advantages), despite behavioral indicators of increased demand and responsibility placed upon the NPS. Almost two-thirds of all responses (64.0%) indicated the belief that no sector should enjoy favor or protection through public policy. More significantly, only 18.0% of responses from informants indicated that the NPS specifically should be protected, demonstrating a very limited base of attitudinal support among home health providers for the claims that the NPS justifies special treatment due to its unique attributes.

Respondents who felt that the NPS should be protected, expressed two general positions:

- a belief that the NPS has better motives and a better interest in providing care than does the private sector; and
- a belief that the care, services, and responsibility to the elderly, and the maintenance of access for disadvantaged populations was better in the NPS.

However the majority who felt that no sector deserved favor or protection were split among a number of ideological positions. The largest percent of responses indicated that, on general principle, no sector should have an advantage over any other. Other categories of responses included those who felt that:

- principles of equality ("everyone should be treated equally", "no favoritism", "it is unfair to discriminate", etc) prohibited differential treatment; and
- upholding principles of the free market (free enterprise, competition and competitive market, etc.) were most important and were threatened by public policy which favored one sector.

Other responses indicated the growing tensions between different types of providers as they try to exist in the current environment. These included many respondents who upheld the relative virtues of one sector as opposed to another ("proprietaries are as good as anyone else", "nonprofits are also profit oriented", and "nonprofits are favored at this time"), indicating that the current cost-containment and competitive environment has both sectors concerned with survivability and changes in their traditional roles.

CONCLUSION

The combination of macro-level challenges to the NPS, across perceptual (ideological), political and economic lines, and our micro-level empirical data argue that the NPS is experiencing a serious challenge to its legitimacy, a situation bordering on crisis. Crisis tendencies are manifested in significant efforts to erode public support for - that is to delegitimate - the NPS as no longer deserving of special status in American society. The structural level conflicts and problems now being waged between the government and business are manifest in present struggles between the NPS, government and the proprietary sector, and these struggles now reach into all major societal and institutional arenas: economic, political and socio-cultural. These conflicts help explain the process of attempted delegitimation of the NPS currently underway. The problems of the U.S. economy, and the response of political conservatism, have rendered the government vulnerable to its own legitimacy crisis. Legitimation problems and public skepticism about government- a popular topic of pollsters and theorists since the mid-1970s- have been attributed to government's inability to meet the dual policy and fiscal demands necessary to promote favorable economic conditions and to redress the social needs of those who are displaced or made redundant by the economic system (O'Connor, 1973). For the NPS as for government, legitimacy challenges raise crucial questions of integrity as well as the very "raison d'etre" of these institutions. Such crisis tendencies result in historical moments when outcomes are uncertain, social struggles endemic, and consequences profound. In this case, the future of the NPS hangs in the balance.

TABLE I

ROLE CHANGES, BY SECTOR (percent)

ROLE CHANGE	NONPROFIT	FORPROFIT	PUBLIC
YES	74%	77%	67%
NO	25%	23%	33%

HHA Q40: "Do you believe that the role of the following types of agencies that deliver health and social services to the elderly in your community has changed in the past three years?"

SOURCE: Institute for Health and Aging Survey, 1987.

TABLE II

TYPE OF ROLE CHANGES, BY SECTOR (percent of responses)

CHANGE	CHANGE IN NONPROFIT	CHANGE IN FORPROFIT	CHANGE IN PUBLIC
INCREASED ROLE	48.4%	51.1%	44.9%
DECREASED ROLE	33.5%	17.8%	43.6%
OTHER CHANGES	18.1%	32.2%	11.5%

HHA Q40a-c "(IF YES) Please explain how this role has changed."

SOURCE: Institute for Health and Aging Survey, 1987.

FIGURE I

INDICATIONS OF LEGITIMATION CRISIS TENDENCIES IN THE NONPROFIT SECTOR

	MACRO	MICRO
SUBJECTIVE/ PERCEPTUAL	1. Formation of IS* 2. Small Business Adm. Report on NPs as unfair competition 3. House Ways and Means Hearings on NP hospitals 4. United Hospital Fund "Mission Matters" Program	1. Limited support for favored status for the NPS 2. increased legitimacy for norms of efficiency 3. increased legitimacy of health as "business" and for profits as service providers
OBJECTIVE/ BEHAVIORAL	Political 1. Legal issues re. income and tax treatment 2. Regulatory changes - restraining advocacy activities of NPS - adding special bidding requirements for NPS 3. Tax reform legislation disincentive for giving Economic 1. Government funding cutbacks 2. Health care cost containment promoting competition between for-profits and nonprofits	1. Privatization of NPS services/activities eg. changing tax status of nonprofits 2. Changing role of NPS - Increased demand/ need by uninsured as "pull" factor - Financial issues as "push" factor 3. Organizational similarities in behavior of NPS and for profits

* The founding of IS reflects both perceptual and behavioral dimensions of crisis tendencies facing the NPS

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PRIVATE HIGHER EDUCATION: PUBLIC POLICY AND THE COMPETITION ISSUE

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PRIVATE HIGHER EDUCATION:
PUBLIC POLICY AND THE COMPETITION ISSUE

Public/Private Differences in Higher Education

Were the topic of concern here public policy toward private higher education over the next six to twelve months, it would be appropriate to plunge directly into currently debated issues. Since this conference is predicated upon long-term assessments, however, it is more fitting to proceed from a perspective based upon the underlying roles and functions of privately controlled institutions of higher education.

In no other industry does the independent sector compete more directly with the public sector than higher education. Although higher education serves multiple purposes, at bottom both privately controlled and government-sponsored colleges and universities ostensibly produce the same product--higher education degrees. In addition, the industry itself is exceedingly decentralized and competitive. The largest producer controls only 1/200 of the customers, and the largest 100 of the 3000+ colleges and universities claim just 22%.[1] A few proprietary institutions on the fringes of higher education pursue, for the most part, highly vocational missions. Otherwise, the industry is divided between independent and public sectors.

The public/independent (or private) distinction refers at bottom to a fact of ownership; from ownership spring fundamental differences in the nature of control and finance; and from those two areas stem differences of purpose and possibilities. In schematic form, these general concepts are related as follows:

$$\begin{tikzcd} & \text{control} \arrow[r] & \text{purpose} \\ \text{ownership} \arrow[ur] \arrow[dr] & & \\ & \text{finance} \arrow[r] & \text{possibilities} \end{tikzcd}$$

Under public ownership, control of an institution is ultimately, but usually indirectly, responsive to the wishes of government. In addition, more than half of revenues for educational and general purposes are provided by state appropriations. As a result, there is a decided orientation in public institutions toward inclusiveness--both with regard to students, in order to provide access, and programs, in order to provide a broad range of services. The possibilities of public institutions are circumscribed by the implicit obligation of making its resources as widely available as is feasible on an equitable basis.

The distinctive position of private institutions can be seen most clearly in opposition to the public pattern. Ownership and control by a self-perpetuating board of trustees permits private institutions to focus upon a more narrow definition of purpose.

Moreover, the sovereignty of the board tends to produce both fixity of purpose over time, and flexibility when circumstances dictate. Private institutions receive more than half of their revenues from student tuition, but their other sources of income are substantially unrelated to enrollment. Their focused sense of purpose assists them to find their appropriate niche in numerous markets--those for students, faculty, research funds, and voluntary support. How they manage to do this, however, will determine the limits of their possibilities. Private colleges and universities as a whole thus, explicitly or implicitly, have an orientation toward selective, non-inclusive definitions of purpose.

Higher education, then, would seem to fulfill Burton Weisbrod's paradigm for the role of the voluntary or independent sector: government institutions basically concentrate upon serving majoritarian demands for educational services; and private institutions derive their justifications and support by appealing to minority tastes and preferences.[2] There is wide latitude for just what kinds of preferences will be reflected in higher education. In the abstract, however, three principal rationales can be identified for departing from majoritarian, tax-supported higher education:

1. high quality/high cost
    - research universities
    - wealthy liberal arts colleges
2. culturally distinct
    - organized cultural minorities (religious sponsorship)
    - consumer preference (secular liberal arts)
3. additional services
    - graduate/professional
    - undergraduate vocational

It is unimportant in this context that individual institutions overlap more than one category, or that some may have fashioned additional rationales: these headings represent approaches to higher education that public higher education, to varying extents, cannot or will not emulate.[3]

In the first category, the claims for excellence, which are ubiquitous in American higher education, are buttressed by the highest levels of per-student expenditures. These are the most expensive institutions, but their students also receive a substantial private subsidy from endowment and gift income. The private research universities, while also nurturing liberal arts colleges, employ their resources to build academic prestige based on contributions to the advancement of knowledge. The twenty or so wealthiest liberal arts colleges direct their resources primarily toward undergraduate education. The high quality of these institutions is unambiguously attested to by the fact that they are the most highly selective in admissions.

Historically, the sponsorship of colleges by religious groups has been fundamental to the development of American higher education. Today, half of all private colleges and universities have religious affiliation, and for most of them this connection is intrinsic to their purpose. It is somewhat more difficult to explain the persistence of the secular liberal arts college. Their current popularity would seem to represent a form of consumer preference for such items as closer intellectual interaction with faculty, picturesque settings, a rich extracurriculum, and membership in a life-long peer group of fellow alums--above all, more active, as opposed to passive, participation in college life.

Private institutions, particularly in urban areas, have generally found a fertile market in providing additional service courses (i.e. programs related to immediate occupational needs). Historically, many cities have been underserved by tax-supported higher education. Many private universities in such settings possess a degree of prestige associated with long-established reputations, and this good standing has enhanced the marketability of their vocational/professional programs. Probably most important, however, has been their flexibility and adaptability as independent institutions, which has allowed them to exploit appropriate opportunities as they appear.

It would obviously be possible to refine this typology with additional subcategories. The purpose in making this breakdown, however, is to be able to relate the principle components of the private sector to recent developments and future prospects.

Numerical Comparisons of Public and Private Higher Education

The private sector became the minority component of American higher education between the two world wars, largely as a result of numerous state normal schools graduating to the status of teachers colleges. A somewhat artificial parity between the sectors was attained in the era of the GI Bill, but after 1950 the expansion of the public sector was far more rapid than that of the private. The disparity in enrollments grew as major state universities increased in size, teachers colleges advanced to become regional state universities, branch campuses turned universities into university systems, and, last but not least, community colleges proliferated. Private institutions expanded as well, generally to the detriment of their fiscal health. When higher education enrollments finally leveled off in 1976, the private sector was left with only 22 per cent of students. It was direly predicted that any further relative shrinkage would deprive the private sector of a meaningful voice in setting higher education policies. Yet, as it turned out, the early [illegible] may have marked the nadir of the private sector in the U.S.

Since the mid-seventies the private sector's share of total student enrollment has remained near 22 per cent, but it has improved its position in most other respects. Its share of [illegible] time equivalent students has risen from 23 to 25 per cent (1975-83); but even that latter figure considerably understates the importance of the private sector. It awards, for example, 33 per cent of baccalaureat degrees. Its share of graduate enrolment has expanded from 28 to 35 per cent (1975-83); and private institutions now award 40 per cent of graduate degrees. In addition, they grant 38 per cent of M.D.s and 63 per cent of law degrees.[4] More importantly (in terms of rising from their nadir), the financial position of private universities has been strengthened substantially during the 1980s.

During the 1970s the private sector as a whole struggled to keep abreast of inflation. Although institutions were able to increase their expenditures greatly, their real level of spending per student was stable throughout the decade. Financial data for the 1980s exists in only fragmentary form, but all indications point to a marked enhancement of all kinds of income.

In 1981 private colleges and universities in the aggregate were able to increase tuition by approximately 5 per cent more than inflation. This basic trend has continued since. As a result, tuition revenues have increased substantially in real terms for the private sector. One up-to-date sampling of private institutions showed real tuition charges to have increased by from 44 to 59 per cent in the past decade (1975-85),[5] and most of that increase certainly occurred in the 1980s.

A second area of financial strength for private colleges and universities has been voluntary support--both present and past (i.e. endowment). Although the proliferation of development efforts in the public sector has resulted in an increasing share of total giving to higher education, the private sector still receives two of every three philanthropic dollars. In the mid-1980s these totals grew dramatically--better than 10 per cent for the 1984, 1985 and 1986 academic years. The current year (1987-88) will probably not be as propitious, but the recent past has presented colleges and universities with an extraordinary opportunity to increase their resources.[6] Endowments too have risen with the approximate doubling of stock market values (post-Crash) since 1982.

External research funding, two-thirds of which comes from federal sources, affects only a minority of private institutions, but the private research universities are a significant minority indeed. Total research funding has risen markedly in the 1980s, reaching the previous peaks of the late 1960s when measured as a percentage of G.N.P.[7] In sum, it would seem that after a decade of difficult times, the basic trends of the 1980s have to date been quite favorable to private colleges and universities. In large measure, however, this prosperity can be related to their basic purposes.

The demand for high-quality/high-cost education has been exceedingly strong in the 1980s. Why this is so undoubtedly depends upon vague cultural factors, such as the waning of the simple-minded egalitarianism and anti-elitism that prevailed in the late 1960s and much of the 1970s. More interesting are the consequences of this phenomenon: the strong demand has placed this set of private institutions in a favorable position to raise prices, and that is exactly what they have done (see below).

The general demand for quality higher education seems to have spilled over to liberal arts colleges in general. Despite the dominant trend toward vocationalism in higher education generally, other tendencies have contributed to the formation of a countercurrent that has made private liberal arts colleges decidedly fashionable (the "preppie syndrome" of emulating old wealth; the value of the extracurriculum; the postponement of inevitable vocationalism to the graduate level). This fashionableness has been considerably abetted by sophisticated and intensive approaches to marketing by the colleges themselves. The liberal arts colleges have much to offer on their own intrinsic merits, irrespective of fashion or advertising. But popularity is helpful as well; and in recent years it has allowed them to ward off the wolf that was at their doors in the early 1970s.

With the service-oriented private institutions it is easier to find economic rationales for their current prosperity. Most urban areas contain widespread demand for a variety of educational credentials that are of value to people already in the workforce. In addition, one of the most efficient adaptations to the escalating cost of higher education has been to study while employed, especially for graduate degrees, thereby eliminating large opportunity costs. Private urban institutions tend to adapt to these markets, while also preserving their other successful missions. Although the provision of these kinds of programs is close to the mission of public-sector institutions, the demand for such services has been robust, and all indications are that it will remain so.

In general, the relative prosperity of the private sector in the 1980s has derived from greater public appreciation for those fundamental purposes upon which their existence is predicated. They have also benefited from propitious economic trends. Perhaps the most important underlying question for the future of the private sector is the extent to which these conditions will persist.

Looking Forward to the Year 2000

In attempting to divine the future, one generally has to make the status-quo assumption--i.e. that most things will stay the same--while also trying logically to identify those things most likely to change. At the same time, one must put aside from consideration such apocalyptic changes that would completely alter the nature of the system. This last assumption is the most perilous. For example, one such system-altering change intruded in the late 1950s with an unprecedented expansion of the [illegible] government; on the other hand, those who expected catastrophic consequences from the decline of college-age cohorts in the 1980s, now seem to have been mistaken.

For private colleges and universities today, the most likely future constant will be stability of purpose. This has been their traditional strength, and, after a period of intense questioning of fundamental purpose in higher education, the developments of the 1980s thus far seem to have reaffirmed the private sector, for the most part, in its traditional roles. The uncertainty, as usual, has more to do with the means.

The financial prosperity of the private sector in the 1980s has been a product both of prevailing economic trends, and of specific government policies. The 1980s has been a decade of privatization in numerous areas of public services. In higher education this has meant a shifting of the burdens of support from government sources to private ones, primarily through the greater relative role of tuition and voluntary support.[8] The effects of privatization have been more dramatic in the public sector, which predominantly rests upon tax-derived funds. Most importantly, privatization has been propelled by the inability or unwillingness of government to maintain or increase its relative support of higher education. A decade ago, when David Breneman and Chester Finn formulated "An Agenda for the Eighties," this development was not apparent: they hoped for combined assistance from both federal and state governments in establishing, through subsidies, an efficient and equitable national pricing system for higher education.[9] Looking in the crystal ball today, one can foresee no significant addition of tax-derived resources for private higher education.

That privatization has been a beneficial trend for higher education to date has largely been possible because of the considerable prosperity of the private economy, especially the financial markets. If the Crash of October 1987 portends anything (and there are those who argue that it does not) it would seem to foreshadow, at the least, less bounteous rewards from those markets and future economic instability--both negatives for fund raising. In addition, with tax cuts in our past rather than our future, it also seems unlikely that personal disposable income--the fluctuations of which are usually matched against tuition levels--will maintain its recent rate of growth. This is one factor that may serve to restrain future tuition increases, but this crucial matter also depends upon public policy in the areas of student financial aid and the public-private tuition gap.

Policy Issues: Student Financial Aid

The private sector has become since the mid-1970s dependent upon federal need-based, or means-tested, student financial aid. In a recent year 63 per cent of independent sector students were receiving some form of financial aid; and 49 per cent of graduates from those institutions owed education-incurred debts that averaged $6350.[10] On the other hand, although these programs are still somewhat controversial in Washington, federal student aid seems to have become a permanent constituent of the panoply of federal responsibilities. Although the Reagan Administration has proposed major amputations, Congress has refused to accede.[11] Nevertheless, the amount of the federal contribution is always an issue.

In the early 1980s (FY1980-1984) the real value of Pell Grants (basic support for the neediest students) declined by 5.7 per cent, and Supplemental Opportunity Grants (subsidizing high-cost higher education) fell by 17.2 per cent.[12] These decreases represent in part an evolutionary shift in federal student aid policy from grants to loans. From 41% of all aid in 1980, loans rose to 52% in just four years. The amount borrowed by college students has increased from $3 billion in 1979 to $9 billion in 1986.[13] In addition, various forms of state aid make a mostly minor contribution to the financial aid picture. More important is institutionally awarded student aid. In 1984-85, student assistance from institutions themselves, which tended to be concentrated in the higher-cost private schools, was almost as large as the total for Pell Grants.[14]

The expansion of need-based student financial aid since 1972 would seem inescapably to have played a major role in facilitating the unprecedented rise in real tuition rates. By subsidizing those students least able to pay higher prices, financial aid allowed colleges and universities to increase tuition without diminishing demand. The most powerful corroboration that this indeed has been the process at work comes from the behavior of private colleges and universities themselves. It has been commonplace for them to allocate approximately 20% of their tuition increases for the provision of additional student aid.[15] Clearly they believe that a multiplier effect has operated. For the private sector as a whole, the growth of need-based student financial aid generally has been multiplied into a much larger increase in tuition revenues.

The rising rates of tuition in American higher education have been led by the country's wealthiest private schools. They collectively establish a tuition ceiling, in relation to which other institutions position themselves accordingly. In the decade 1975-85 private sector tuition increased by 152%, while the ceiling tuitions rose 180%.[16] The difference between those two percentages represented more than $1000 in annual tuition for a Harvard student. For this group of institutions the composition of the student body, and hence the recruitment pool, is one of the most critical factors of institutional existence. Rising tuition has apparently not diminished these recruitment pools because of relatively large amounts of institutional student aid. But, how much longer will this spiral of increasing student aid multiplied into even greater institutional tuition revenues be continued?

It seems unlikely that the aid-tuition spiral can be as effective in raising private sector revenues in the future as it has sofar during the 1980s. Each of the three components--tax-derived grants, government-backed loans, and institutional aid--face somewhat different constraints. Government spending for student grants will likely stabilize at best, if in fact the current real downward slide is stemmed.. Where the limits of student indebtedness lie is more difficult to predict; however, the current levels appear to be dangerously high. To shift the burden of financing higher education even further onto students could well produce a decrease in demand, especially in the private sector. As for institutional aid, it depends heavily upon fund raising, which in turn is sensitive to the economy. Both of these last two sources may have some room for additional growth, but as a component of the finance of higher education, student aid would seem to have reached the stage of maturity in which relative expansion will be minor. If this is the case, it also seems unlikely that tuition increases in the private sector can continue to outpace inflation.

The Tuition Gap Revisited

The financial difficulties facing higher education from the late 1960s into the 1970s caused an intensive national scrutiny of basic funding issues. The concrete result--the Educationa Amendments of 1972--largely confirmed the existing system by channeling additional federal funds through students. Nevertheless, one of the recommendations consistently made during this period was for an increase in the charges for public higher education. One study recommended that public-sector students pay one-third of the cost of their education; another suggested they pay one-half.[17] For economists it appeared that the largely middle-class constituencies of public higher education were being overly subsidized, and that some of this subsidy might be more equitably transferred to need-based aid.[18] Such a policy would also have been theoretically beneficial to the private sector by raising the public side of the tuition gap.

State-supported institutions do not seem to have raised tuition in response to these abstract arguments, although a few eventually adopted indexed rates of tuition. Instead, states have tended to raise tuition in response to fiscal stringency.[19] Since 1979 increases in public-sector tuition have been just inferior to those for the private sector. For the decade 1975-85, public sector tuition increased by 140% (vs. 152% private); and its contribution, as measured against expenditures for instruction and academic support, rose from 30% to 37%. Unfortunately, the gap keeps growing in absolute terms. In 1964 the tuition gap between private and public universities was $1000; by 1974 it had risen to $2000; in 1979 it reached $3000; and in 1985 it was $6000 (nationwide averages). In 1987 the gap between a ceiling-level private institution (c. $12,500) and a major state research university was more than $10,000 for an in-state student and about $7000 for an out-of-state student.

It has been common to find solace in these figures by adding to tuition the costs for room and board, plus opportunity costs, which are the same in both sectors. This makes the disparity in cost much less in percentage terms. These costs can then be measured against rises in family income to prove that people can still afford private higher education. However, as Michael MacPherson has warned, "ability to pay cannot necessarily be equated with willingness to pay."[19]

As was seen above, the willingness to pay for high-quality/high-cost private higher education has been abundantly present in the 1980s. In general, the widespread appreciation of the importance of quality in higher education seems likely to persist into the immediate future. The principal beneficiaries of the current market environment have possibly been state research universities, which in some ways offer considerable quality at a moderate price. As their applications have soared, however, they have become far more selective. Much of private higher education remains competitive within the general market for full-time, away-from-home students. Many private institutions currently charge from $6000-9000, which is only slightly more than out-of-state rates at public institutions. Beyond this lies the vast market for low-cost, largely local public higher education. Although private institutions once played a vital role in providing this kind of access to higher education, they have ceded this role to state and community college systems.

Today the private sector can probably look to the future with less trepidation than at any time in the last two decades. The chief negative factor that must be faced is that the favorable financial trends of recent years, which have allowed private institutions to increase charges at more than twice the rate of inflation since 1982, will not persist. This year, next year, or some year thereafter, will bring the onset of a more austere economic environment. But most private institutions strengthened themselves considerably during the fat years. They have reinvested a substantial portion of their additional revenues in admissions, student aid, and development--areas intended to yield a continuing return in enrollment, revenue and gifts. Moreover, the current funding arrangements for higher education stand a good chance of being viable over the long term. Although student aid may not show much further increase, it probably represents a permanent price support for private-sector tuition. Other factors too point to further stability. The roles of the public and private sectors would seem to be growing more complementary and less competitive. In the year 2000, then, the American private sector will probably be similar in role, dimensions and finance to its profile today because, in the waning years of the twentieth century, as in the past, the chief strength of the independent sector will be the stability of purpose of private colleges and universities.

NOTES

1 All statistics, unless otherwise noted, are from the *Digest of Education Statistics, 1985-86*.

2 Burton A. Weisbrod, "Toward a Theory of the Voluntary Nonprofit Sector in a Three-Sector Economy," in *The Voluntary Nonprofit Sector* (Lexington, Mass.: Lexington Press, 1977).

3 The three rationales for private higher education are developed in, Roger L. Geiger, *Private Sectors in Higher Education: Structure, Function and Change in Eight Countries* (Ann Arbor: University of Michigan Press, 1986).

4 Center for Education Statistics, *State Higher Education Profiles: 1985* (Washington, D.C.: GPO, 1987), 10.

5 Michael O'Keefe, "Where Does the Money Really Go: Case Studies of Six Institutions," *Change* (Nov./Dec. 1987), 12-34.

6 See the annual reports of the Council for Financial Aid to Education: *Voluntary Support of Education*.

7 National Science Foundation Data (preliminary).

8 Roger L. Geiger, *Privatization of Higher Education: International Trends and Issues* (Princeton, N.J.: International Council for Educational Development, 1988).

9 David W. Breneman & Chester E. Finn, Jr., "An Agenda for the Eighties" in idem.,eds., *Public Policy and Private Higher Education* (Washington, D.C.: The Brookings Institution, 1978), 411-50.

10 National Institute of Independent Coleges and Universities, "The New Economics of Independent Colleges and Universities," (NIICU, 1985); Cathy Henderson, "College Debts of REcent Graduates," (American Council on Education, Dec., 1987).

11 For example, the President's budget request for FY 1988 proposed to eliminate all funds for College Work Study and Supplemental Grants, but these programs were funded by Congress with miniscule reductions: *Chronicle of Higher Education*, (1/6/88), A17.

12 D. Bruce Johnstone, *Sharing the Costs of Higher Education* (New York: College Entrance Examination Board, 1986), 139.

13 Ibid., p. 139.

14 Ibid., 131.

[15] O'Keefe, "Where Does the Money Really Go."

[16] Ceiling = average tuitions at Harvard, MIT and Princeton.

[17] Carnegie Commission on Higher Education, *Tuition* (Berkeley, Cal.: CFAT, 1974).

[18] Michael S. MacPherson, "The Demand for Higher Education" in Breneman & Finn, *Public Policy*, 143-96.

[19] E.g., David J. Berg & Stephen A. Hoenack, "The Concept of Cost-Related Tuition and Its Implementation at the University of Minnesota," *Journal of Higher Education* 58,3 (1987):276-305; Geiger, *Privatization of Higher Education*.

[20] MacPherson, "Demand for Higher Education," 173.

WORKING DRAFT

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CHALLENGES IN EDUCATION FOR CITIZEN PARTICIPATION

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Challenges in Education for Citizen Participation

If we are relying on our educational institutions at the secondary level to prepare students for informed participation in American society in the year 2000, then we will be sadly disappointed. Instead of preparing students to become active, involved citizens, according to one recent survey , our civic and government textbooks are preparing "students to be bystanders". Anthony Podesta, President of the People for the American Way, said that his organization did a survey of 18 textbooks and found that...

> Eighty per cent of the civics books and half of the government books minimize conflict and compromise. The dynamic sense of government and politics-fierce debates, colorful characters, triumphs and tragedies-is lost...Voter turnout among young people is abysmal. Textbooks about our democracy should inspire students to become active involved citizens. Instead, these books prepare students to be bystanders in history.[1]

Gilbert Sewall, a researcher at Teachers College of Columbia University, concurs with this assessment. He adds, "American history textbooks often forsake good storytelling, energetic writing and even honest history to comply with adoption procedures, group pressures, the social studies approach, readability formulas and other market forces."[2] A recent study of college students done by Alexander Astin, and cited by David Matthews, in an article on civic intelligence "...only about 40 per cent, far less than half of the next generation are interested in public affairs or the great issues of the day. Only 20 per cent, one out of five are likely to become involved in helping other people in some form of community activity. On-campus speakers who discuss how to play the stock market or become "computer literate" draw crowds; those who discuss social issues speak to an empty house."[3]

There is no quick fix or formulaic response to this problem. But there are alternative paths which can be pursued in order to develop viable models for citizenship education. At **Facing History and Ourselves** the Choosing to Participate project, through its approach to curriculum development and teacher training, is pursuing another direction in this area. This effort is not an attempt to over turn centuries of educational theory, but rather to highlight some of the individuals and groups which have often times been left out of the textbooks, but who have nonetheless helped shape our democratic inheritance today.

Throughout American history, educators have debated ways to define and improve civic education. Progressive educators in the 1930's advocated social participation for all students. Paul Hannah's curriculum solutions for the Depression years echo those of today who believe children learn to be socially responsible by practicing democracy and by experiences in governing themselves. Hannah argued, "that children had an obligation to contribute to the solution of the great social and economic problems of the nation, not by merely understanding them, but through social participation."[4] In the 1940's, a Harvard Committee of educators emphasized the study of history through philosophy and literature as necessary for bringing goodness to our society. Albert Einstein extended this thinking in the 1950's when he said,

> A good education will teach young men and women the importance of independent, critical thinking.
>
> ...It is essential that the student acquire an understanding of and a lively feeling for values. He must acquire a vivid sense of the beautiful and of the morally good.
>
> ...He must learn to understand the motives of human beings, their illusions and their sufferings in order to acquire the proper relationship to individual fellow men and to the community... This is what I have in mind when I recommend the 'humanities' as important, not just dry specialized knowledge in the fields of history and philosophy.
>
> Overemphasis on the competitive system and premature specialization on the ground of immediate usefulness kill the spirit on which all cultural life depends, specialized knowledge included.[5]

Yet, we hear from some in the 1980's, that philosophy and the humanities should best be left to the few, the "elite", in special university settings who will contemplate inwardness away from the problems of the world.

While the debate about who is best suited to study philosophy is usually reserved for the college level, secondary schools are responding to those who call for vocation or pre-professional training for most secondary students. Harry Boyt, Director of the Public Philosophy Project at the Humphrey Institute, criticizes this trend as limited, "... the language of civic commitment and virtue has been largely replaced by a narrow, technical and careerist vocabulary of education..."[6] Though the debate about extremes draws some attention to the role of education in America, the more thoughtful outcomes will probably come from the innovative educator who recognizes and tries to balance the need to understand and think about ones life as a citizen in a community and the need to prepare the labor force. Hannah Arendt, a 20th century philosopher, has spoken to this challenge. Leon Botstein, President of Bard College, restates her idea, "Unlike labor, which is an alienating process, work is compatible with her desired ideal of the active life. The ideal *vita activa* calls for speech and action in the public realm, for the virtuous display of freedom by individuals on behalf of the human community."[7] It is clear she expresses the importance of work as well as emphasizing the active participation of each citizen to insure the health of the community.

Even with these efforts to recognize the failings of civic education, the efforts to improve it have not been encouraging. Fred Newman, Director of the National Center on Effective Secondary Schools, offers these ideas on the problem.

> Both mainstream and reform programs have failed for three reasons: first, compared to other goals of education, our society refuses in practice, to place citizen education as a high priority; second, the curriculum offers inadequate attention to issues central to democratic citizenship in a mass modern society, and it denies students the opportunity to confront these issues through experience; and finally, reforms that have addressed these issues have been impotent because they have issued pronouncements, programs, and texts without developing a sense of ownership among teachers, who shoulder the major educational responsibilities...
>
> Most evidence indicates that numbers of citizens lack the implied commitment, understanding, and skill. If, by definition, democracy demands a citizenry educated along these lines, then citizen education must be improved.[8]

Recognizing that most teachers will use the inadequate textbooks and that thoughtful in-service education for teachers is not likely to happen across this nation, reformers are looking for new avenues for enhancing the education of teachers and their students. Many of these innovations aim to address the topics of this forum for the secondary level by reasoning that the study of America's unsung traditions of volunteerism and philanthropy should take their place in the study of American society along with the history of government and the business economy. The study of voluntary and non-profit service and advocacy it is argued will not only enhance ones notion of citizen participation, but rediscover those individuals and groups, often blacks and women, who have practiced self help, advocated change, and used the protections of the First Amendment to challenge and claim the promise of America's democratic society.

As a national educational foundation, **Facing History and Ourselves** has focused on the lessons to be learned from an examination of the Holocaust, a case study where a democracy failed and neighbor turned against neighbor. After students have studied this history many of them ask what choices are available to them so they can make a difference in their own society. The Choosing to Participate project encourages students to look at the history of the United States as a way to better think about this question. Through its approach to curriculum development and teacher training the project highlights some of the individuals and groups who have been often left out of the textbooks, but who have, nonetheless, helped shape our democracy. The project shows how people- as students, citizens, volunteers, and paid workers- can reach beyond themselves to develop goals and consider their shared responsibilities. It is a serious inquiry into the role voluntary associations and philanthropic activity has played in American society, allowing students to see how some of our basic democratic ideals have evolved over time and reaches their lives today. Harry Boyt, underscores the importance of examining the third sector in promoting civic awareness in our students today. He says, "Voluntary associations have not only taught a deepened regard for the common good of communities, as Tocqueville argued. They have also proven a vital meeting ground where people of diverse background, viewpoints and outlooks could become acquainted and learn an ethos of mutual accountability and practices of cooperation."[9] When students can study these kind of examples it is our hope they will develop a better understanding of how they can participate more fully in our society and balance the needs of self and others.

This sentiment really gets to a central question that has concerned **Facing History and Ourselves**, and we believe intrinsic to the study of citizen participation, which is the examination of the relationship of the individual to society. This kind of thinking about self and other is an aspect of what David Matthews, refers to as civic intelligence. "Being civically intelligent means having the capacity to find out what the facts are and what the facts means to others."[10]

An understanding of the democratic institutions and protections which help us grapple with the proper balance between individual rights and our responsibility to others will help push students thinking beyond their private concerns. This focus rooted properly in philosophy, where ethical questions guide our thinking about choice and action, can be learned best through examining the stories of men and women who acted as historical characters.

These case studies, illuminating the every day heroes and heroines, who are part of the undervalued associations of individuals that make up the history of American democratic citizenship, help students understand their role as productive citizens in a democratic society. In essence students have to take themselves seriously historically. According to Bill Moyers...

> The problem of democracy is the problem of the individual citizen who takes himself or herself lightly historically, no matter how bloatedly one might take oneself personally. By that I mean if you do not believe that you can make a difference, that you matter, you're not going to try to make a difference, you're not going to try to matter, and you will leave it to someone else who may or may not do what is in the best interest of your values or of democracy's values.
>
> I find increasingly frustrating the student who comes to me and says, "Well I just don't really believe anyone does matter," and I say "Shame on you for taking yourself so lightly historically." You have to realize how, brick by brick...a nation is built, a city is built or a society is sustained.
>
> Unless students today realize that-the school, the church, the synagogue, the library, the street, the park, the television screen, that everything we have comes to us through the contribution of others over time from the past-then how is the student going to realize, "I have to help build the next school or the next church or synagogue or the next library, or the next book on the shelf or the next television broadcast."?[11]

Based upon our experience of working with adolescents learning history we have found there is an untapped potential for them to extend their thinking toward more mature notions of what it means to be a responsible citizen in a democracy. As Matthews tells us, "the word 'public' is rooted in pubes, the word for maturity, implying a people with the capacity to understand the consequences of individual actions on others, the capacity to see beyond the personal."[12] We agree with Matthews and Moyers; we take students very seriously, maturity or citizenship is not something we take for granted. It is something we have to work at.

Because adolescence is a time of heightened moral awareness, the ethical content of certain questions attracts the attention of high school students. The questions of who gives and who gets in our society echo teenagers' concerns about who's in and who's out, power and helplessness, care and indifference. If students are to participate in answering the questions that face our society, than we must hear, confirm and develop that sense of justice and care. By focusing on American traditions of participation, students can learn that individual and group involvement can influence their schools, communities and larger democratic society. The Choosing to Participate project aims to help students learn how people choose to become involved and why participation is important. Students will be encouraged to reach beyond themselves to consider the needs of others and their own responsibilities for imagining and creating the future.

In pushing students to think beyond their own immediate concerns Facing History prepares students to tolerate ambiguity because there are not always clear cut and simple answers to complex questions confronting us in society. The lessons being developed for the Choosing to Participate resource book encourage students to critically reflect on situations before giving quick judgments. Students need that opportunity to engage in what Hannah Arendt has termed the "soundless dialogue" in ones own mind, where we question our own preconceived notions about a situation. This is to be what Socrates refers to as "perplexed", purging ourselves of "unexamined prejudgments which prevent thinking."[13] Once students examine their own thinking about a subject they are better able to critically listen to other opinions and eventually make informed judgments on their own. The project believes that a sound civic education provides students with the tools by which they can weigh various perspectives before they make their choices to act responsibly.

Toward this end the resource book uses the case studies and examples from the voluntary tradition and non-profit activity in American history to stretch students' notion of self and other, and hence deepen their thinking about what constitutes civic responsibility. In this resource book being completed for teachers and students readers are first introduced to questions of motivation , asking the question why do some people choose to act for others? The first chapter exposes students to a variety of readings which focus on real life situations of young and old, past and present, who exhibit a range of human behavior. In reading about situations where some people are bystanders or others go out of their way to care for those in need lessons are provided to encourage students to think beyond easy answers and ponder the complexities of human motivation. Questions of what constitutes universal moral behavior versus considerations of cultural relativism are introduced in these lessons. For example, lessons are developed about what it means to give and receive a gift in certain cultures, leading to an exploration of universal and unique notions of reciprocity and obligation.

These early readings begin to serve as a way for students to reflect on their own thinking about what they might have done in a similar situation or what is actually going on in their life today. As a way to help frame this thinking, students are introduced to a new vocabulary which includes such words as altruism, charity, and philanthropy. These terms continue to be revisited throughout the other chapters in the resource book as a way of getting them used to the idea that they have a place in how we examine fundamental aspects of human behavior. The rest of the book builds on these concepts and provides more of a philosophical and historical context for their role in American society.

Once students are engaged in thinking about questions of motivation other chapters extend these concerns into other areas. For example how have we as a society developed notions of responsibility from the colonial times to the present? Students read about how early efforts at poverty relief were often sponsored by local community and religious groups, which were later followed up by the charity organization societies of the 19th century. These readings are built around the ideas and actions of men and women who were grappling with challenges that are still with us today. In representing the ideas of Benjamin Franklin and Cotton Mather or the actions of the "friendly visitors" practicing scientific philanthropy there is not an attempt to romanticize the voluntary tradition. All too often text books practice what Michael Kamen, a historian a Cornell University, calls "heritage nostalgia (which) freezes history into a vague golden time, and the tension, paradox, and triumph that are the truth of the past become lost."[14] Indeed when students read about the settlement house movement of the early 20th century and compare current programs of poverty relief they realize that public policy toward helping those in need has been part of an evolving debate over the years and that tensions within the sector and between it and government and business form a necessary part of participation in American democracy.

The notion of history and change also figures prominently in the book. One of the case studies students look at in this section is the early civil rights movement. They are first introduced to story of Ida B. Wells and the anti-lynching movement in the 1870's. This kind of example from the voluntary tradition exposes students to the role gender and race have played in the history of this country, areas which are often under represented in traditional textbooks. By reading about the frustrations and setbacks this woman encountered in combating some of the social evils in the age of Jim Crow, students realize change does not come over night, but through the work of those who came before and those who will follow in the future. This idea is emphasized in the middle of this story when students are introduced to the efforts of the abolition societies decades before Ida B. Wells helped begin the anti-lynching movement. Students begin to see how she was able to build on the traditions and associations utilized by the earlier abolitionists. Also, students read about the role philanthropists played in aiding the movement she helped lead. They see how many of the key philanthropists and activists from this movement continued the struggle for social justice into the 20th century through their financial and volunteer contributions to the newly founded N.A.A.C.P. Students begin to appreciate how these individuals and associations have laid the moral foundation for what eventually would become law and government policy.

When students examine case studies from the civil rights movement, such as the anti-lynching campaign, or the settlement house experiments of the Progressive Era, they are seeing the vital and dynamic role independent associations have played in helping this country better realize its democratic ideals. In this way the resource book is addressing a problem Gilbert Sewall has noticed in the teaching of American history. "Textbooks should face historical conflicts and tensions squarely, outlining them in strong and dramatic prose, not shrinking from class, religious, racial or gender controversies for fear of giving offense to potential book buyers."[15] They read about how the modern foundation developed and its importance in sustaining and initiating projects which were addressing the social and economic needs of this country. Reading about these examples underscores how our basic freedoms as outlined in the Bill of Rights have been kept alive by the persistent efforts of individuals and groups associating in ways that go beyond the activity of government and business activity.

Finally, students are presented with examples and models for participation in their lives today. The earlier questions on motivation, responsibility, and change are brought to fruition in the last two chapters. In the chapter on political participation students are asked to consider the civic dimensions of political activity when they analyze case studies on the property tax revolt and nuclear waste disposal. They look at forms of involvement that go beyond mere voting or descriptions of the branches of government. Here they examine the role community associations and non-profit organizations play in mobilizing people to act on issues. The last chapter portrays young people helping set up shelters for the homeless, working in community service clubs, or putting their energies into global concerns by joining Amnesty International or working on world hunger. The earlier questions about why should you act, how do you choose where to act, and how do you know you are making a difference confront the students in these readings. But now students have a historical template for looking at themselves and their society today. Students now have examples to draw upon from the history of their own nation, illustrating how people before them grappled with these questions, and helped to point the way for how they can think about them today. Both the past and present case studies offer students a way of thinking about civic responsibility through exposure to the independent sector and as a result have a better understanding of the choices available to them.

As important as it is to make accessible to students the reading material which complicates their notion of civic life, **Facing History and Ourselves** realizes there is another important dimension for reinvigorating citizenship education. Paul Gagnon, writing in the report, Democracy's Untold Story, speaks to this point.

> We understand that such a major reform of the curriculum will require more effective textbooks and auxiliary materials, aimed less at "coverage" than at comprehension of what is most worth learning. It will require continuing collaboration between faculty members from the schools and universities, where both work together as equals to clarify what is most worth teaching in their subjects and to devise ways to convey the material to diverse clienteles. And it requires new approaches to teacher education, both pre-service and in-service, to help teachers present the revamped and strengthened curriculum.[16]

Facing History and Ourselves has always attempted to act as an liaison between scholarly research and adult learners, who usually are school teachers. This has certainly been true of the work we have done on the Choosing to Participate project. An Advisory Board was formed, with representatives from a cross section of the nonprofit and philanthropic community who contributed to the project's vision and direction. For example, the ideas of Kathleen McCarthy on noblesse oblige have proved invaluable for how we have presented the history of charity and philanthropy in the resource book. Interviews were conducted with a variety of individuals whose experience and knowledge helped inform the project: Brian O'Connell of the Independent Sector, Lester Salamon of the Urban Institute, and John Simon of PONPO have been some of the people who contributed their expertise. We have also been participants in symposia, such as the Humphrey Institute's forum on "Renewing the Commonwealth" where we have kept abreast of some of the latest thinking and research in the non-profit field.

We have attempted to translate these scholarly contacts into ideas for the resource book and into our professional development efforts with practicing teachers. The resource book includes an extensive flimography of edited videos designed for use with the curriculum. The book and videos have the potential to be shared with our vast network of school contacts. Facing History has worked with more than 30,000 educators who reach 450,000 students annually in 46 states across the country and in Canada. Through this network and from publicity given the project in our newsletter and educational journals we have begun to conduct intensive introductory and follow up workshops. The continual support and training of teachers is a keystone to our development of educational programs. Providing teachers the resources and professional time to think about the issues raised in the project makes for greater ownership on the part of the individual teacher and therefore for better comprehension on the part of the student.

At present we are field testing the materials in a number of pilots across the country. These include the Youth Community Service clubs of the Constitutional Rights Foundation in Los Angeles, inner city and suburban public school classrooms, and independent and parochial schools in various parts of the country. Working with teachers in workshops, through site visits, or over the telephone is an integral part of making any curriculum on civic education occupy a valuable place in a school community. In each situation we encourage teachers to document their student responses to the lessons being taught from the resource book. In return teachers begin to perceive the project as a valuable way for enhancing skills that are vital to the debate and dialogue of a democratic community within the classroom: critical reading and listening, gathering information, presenting ideas, and respecting other's opinions. As the nation continues to mark the anniversary of the Constitution and Bill of Rights, these skills and the project's content can help educators make these commemorations an opportunity for a rigorous exploration of what this heritage has meant for our lives today.

The real life stories of people who have worked to achieve a better civic culture have used avenues of association that are not just government or business. Our challenge is to bring these case studies into the minds of students and help explain how they are part of the history that have shaped our society today. And the activities of people who are part of this tradition are inspired by time honored philosophical ideals. Indeed, for students to feel they can make a difference, a comprehensive civic education must be rooted in the soil of philosophy and history.This will not be any easy task because our students can be distracted by other powerful forces in our culture. Benjamin Barber despairingly labels these as "the nation's true pedagogues-television, advertising, movies, politics and the celebrity domains they define."17 How well we meet this challenge will tell us what the year 2000 will bring.

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2. Muriel Cohen, "Study Finds Distortions in History Books," The Boston Globe, (Oct.21, 1987), p. 11.

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4. Dianne Ravitch, "Tot Sociology: What Happened to History in the Grade Schools," The Key Reporter of Phi Beta Kappa, (Autumn 1987), p. 2.

5. Benjamin Fine, "Einstein Stresses Critical Thinking," The New York Times, (October 5, 1952), p. 37.

6. "A Symposium on Renewing the Commonwealth," The Antaeus Report, (Spring 1987), p. 12.

7. Leon Botstein, "Hannah Arendt:The Jewish Question," The New Republic, (Oct.21, 1978), p. 34.

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10. Matthews, op. cit., p.680.

11. Bill Moyers in "Brick by Brick: Seeing Yourself Historically," (Unpublished draft of Choosing to Participate resource book, **Facing History and Ourselves**), Reading 7, p. 1.

12. David Matthews, "The Independent Sector and the Political Responsibilities of the Public," excerpts reprinted in Facing History and Ourselves News, (Summer 1987), p. 12.

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17. Benjamin Barber, "What Do 47-Year-Olds Know?," The New York Times, (Dec. 26, 1987), p. 23.

WORKING DRAFT

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THE PROBLEM WITH "NEW" MONEY: GOVERNMENT LEVERAGE OF PRIVATE SUPPORT FOR NONPROFIT ORGANIZATIONS--THE CASE OF THE ARTS

by

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INTRODUCTION

Government agencies that support the activities of nonprofit organizations are increasingly turning to matching grants to leverage increased private support. In no sector has the matching grant become as popular as it has for the arts and culture. This is true because the public sector is increasingly reticent to decide which artistic and cultural activities are worthy of support, decisions that involve unusually vague criteria of aesthetics and innovation and which touch on issues of censorship. It is also true because the arts have demonstrated appeal to private support, particularly from the corporate sector, an argument that is borne out by charitable statistics. And, finally, in a era of privatization and public-private partnerships--a trend both across nonprofit sectors and across a wide range of countries--the notion of combining public and private sources of support has considerable ideological appeal.

In analyzing matching grants it is helpful to distinguish between three different forms of matching grants that correspond roughly to the historical evolution of such grants. Governments in the United States have been the foremost proponent of matching grants, and the "American model" serves as the model for many of the new matching programs in other countries. From the very beginning, the National Endowment for the Arts has followed the principle that it will not fund the total cost of any project; its enabling legislation specified that it could only provide up to 50 percent of the cost of any project it supported.(1) Thus, co-financing became the first, albeit implicit, matching grant, and other funding sources were expected, if not required, to match or complement the federal grant. More recently, the Endowment has used explicit matching grants throughout its funding programs, most notably in the Challenge Grant program in which the recipient organization can free up one dollar of its Challenge Grant for every three dollars in new contributions from other sources.(2) The term challenge grant is a useful one to describe this type of matching grant because the government agency has made an explicit decision to challenge a particular arts organization to increase its fundraising. Arguably, the challenge grant is the most familiar form of matching grant.

The most recent matching grant programs, however, have taken on a new form, particularly when those matching grants have been targeted at increasing corporate support. These matching grants might be called reverse matching grants in that they promise that the government will match, more or less automatically, increases in private support of the arts. There is no government selection of the matching grant recipient beyond the broad determination of eligibility criteria. These grant programs reverse the logic of the traditional matching grant; they allow the private donor to make resource allocation decisions that are followed, rather than led, by the public sector's match.

The National Endowment for the Arts has not yet used reverse matching grants, but they have been used at the state level, and they have recently become popular at the provincial level in Canada and at the national level in Great Britain and France.(3) Three reverse matching grant programs have been in existence long enough to illustrate the issues that funding the arts through matching grants raises: the Regional Corporate Challenge Program in Massachusetts, the Wintario Challenge Grant and the Investment in the Arts programs in Ontario, and the Business Sponsorship Incentive Scheme in Great Britain. Some of the more important attributes of these three programs are summarized and compared in Table 1. In this short paper I am unable to capture all of the interesting nuances of these programs. Rather, I will use these three programs to serve as a background to suggest the difficulties inherent in government matching grants as a source of support for nonprofit organizations as well as to illustrate new issues posed by reverse matching grants.(4)

WHY A MATCHING GRANT?

What is the theory behind matching grants? Why do governments turn to matching grants as opposed to unencumbered grant support as the chosen instrument of government policy? Possible theoretical justifications include:(5)

- TESTING LOCAL DEMAND--Particularly in new areas of government intervention, a higher level of government may wish to test the degree of local commitment to a project as measured by its willingness to spend local resources. In this way implementation may be better assured. To be sure, it is not only governments that initiate matching grants to test local demand. Andrew Carnegie, before providing communities with a Carnegie Foundation grant to build local libraries, insisted that they would have to raise from taxes an annual amount for maintenance equal to one-tenth of the grant.(6)

  Netzer has criticized NEA's support for state arts agencies on these grounds.(7) The Federal/State Partnership Program was intended to provide an incentive for the creation of state arts agencies through federal matching grants to each of the states. Through the 1970's many states failed to fulfill their matching requirements; yet the NEA funds were allocated, despite the fact that the test of local demand was not met.

  The increasing popularity of matching grants has made testing local demand problematic because of matching grant congestion. Multiple matching grants made in one geographical area have led to "saturation," prompting vigorous competition among groups for limited local philanthropic resources.(8)

- LOAD SHEDDING--The combination of limits on public resources and the increasing shift toward privatization of previously public programs has led governments to shed programs, often with the assumption that they will be picked up by the nonprofit sector (another, more direct test of local demand). A matching grant might provide a transition by attracting the private resources to make load shedding supportable.

Table 1: Comparison of Reverse Matching Grant Programs--Massachusetts and Great Britain

Program:	Massachusetts Council on the Arts and Humanities Regional Corporate Challenge Program	Office of Arts and Libraries, Great Britain Business Sponsorship Incentive Scheme
Dates:	January 1983 - December 1986	October 1984 -
Goals:	To increase the total dollars given by the business community to the arts, to broaden the base of funders as well as the number of recipients of corporate giving, and to develop a network of interested business-people statewide who would become advocates for the arts in their communities.	To attract new corporate sponsorship of the arts by offering a measure of government endorsement and financial support.
Eligible Organizations:	Any Massachusetts arts institution that had received some funding from the Council in any year since the fiscal year preceding the creation of the Committee in its region. For a region to be included in the program it had to have at least six eligible institutions and a Regional Business Committee.	Originally, any "bona fide arts organization" (including commercial). Now restricted to organizations that have charitable status, that are not profit-distributing, or that receive government funds. [Includes organizations that are ineligible for support from the Arts Council of Great Britain.]
What is Matchable? ("New" Money)	Original program design was to match net increases in the aggregate of corporate cash contributions for general operating support in each region with a Regional Business Committee. Eventually, three more costly variations on this rule appeared: matching the net increase in aggregate giving by any member of a Regional Business Committee, matching the net increase in corporate contributions made to a particular institution, or matching the net increase in giving by a particular corporation to a particular organization.	Increases in corporate sponsorship. Each arts organization can claim a match for one sponsorship per year.
Ratio of Match:	$1.00 Gov't Match : $1.00 Matchable Corporate Donations Originally the match was to have been subject to an upper limit set by the approved annual fundraising goal for each Regional Business Committee (and used to budget for the program).	Original Rules 1 pound Gov't Match : 3 pound increase in Corporation's Total Arts Sponsorship Increase had to be at least 7,500 pounds with a maximum increase of 75,000 pounds for each sponsorship matched. Current Rules For first time sponsorships of 1,000-25,000 pounds by a business that has never sponsored the arts before: 1 pound Gov't Match : 1 pound Sponsorship For existing sponsors who increase their total annual arts sponsorship by 3,000-75,000 pounds: 1 pound Gov't Match : 3 pound increase in Corporation's Total Arts Sponsorship (Each sponsorship matched must have increased by at least 3,000 pounds.
Total of Gov't Match:	$2.36 million over four years of program.	3.25 million pounds over first 30 months. 1.75 million pounds budgeted for current yr.
Constraints on Use of "New" Private Money:	Ongoing operating expenses.	Expenses of the sponsored project.
Constraints on Use of Matching Money:	No restrictions, though it was hoped that organizations would not budget expected matches into their ongoing budgets.	Use Match is "intended to be used in some part to enhance the sponsorship,...ensuring increased benefits for the sponsor."
Required Documentation:	Annual request for match prepared by each Regional Business Committee and reviewed by Council staff.	Detailed application form filled out by arts organization and sponsor. Arts organizations required to provide audited accounts showing that the match has been used to enhance the value of the sponsorship to the sponsor.
Involvement of Intermediary Institution:	Regional Business Committees required for a region to participate in the program. Committees were eventually created in eight regions, three of which were set up as United Arts Funds. Boston excluded from program.	BSIS is administered for the Office of Arts and Libraries by the Association for Business Sponsorship of the Arts, a non-governmental, nonprofit organization.

Table 1: Comparison of Reverse Matching Grant Programs (continued)--Ontario

Program:	Ontario Ministry of Culture and Recreation Wintario Arts Challenge Fund	Ontario Ministry of Citizenship and Culture Investment in the Arts
Dates:	June 1980 - March 1983	June 1986 -
Goals:	Encourage major nonprofit arts organizations to achieve greater longterm financial stability by: - Assisting in establishment of an investment (endowment) fund to provide longterm operating income, - Increasing current level and broadening base of private/corporate support, - Acting as an incentive toward elimination of accumulated deficits, and - Benefiting arts organizations without creating a dependency on lottery or tax funds.	To help Ontario-based non-profit arts organizations receiving provincial support achieve longterm financial stability by: - Eliminating reducing accumulated deficits and balancing current operating budgets, - Encouraging greater donations from the public and corporate community, - Encouraging the development of more sophisticated fundraising techniques and financial management capabilities through the provision of matching incentives and endowment fund management requirements, - Providing support for northern arts organizations, and - Supporting arts organizations in obtaining new corporate donors.
Eligible Organizations:	Ontario arts organizations with operating budgets > $250,000, which already were receiving annual assistance from the Ontario Ministry of Culture and Recreation or the Ontario Arts Council. [35 organizations]	Ontario arts organizations with operating budgets > $75,000 which have been in existence at least three years and are currently receiving annual assistance from the Ontario Arts Council, and Arts Service Organizations supported by the Ministry of Citizenship and Culture. (> $50,000 budget for art schools providing professional training, cultural centres, and arts organizations in northern communities.) [220 + organizations.]
What is Matchable? ("New" Money)	Individual, business, and foundation donations above the "base fundraising level," determined by calculating the average percentage of operating income raised through private fundraising in the previous 3-5 years and multiplying that percentage by current year's operating expenses.	Same calculation (based on three previous years). Only cash donations are matchable. Restrictions on matchability of donations from foundations or other bodies related to applicant institution. Funds raised for a capital project or to satisfy any previous Wintario matching requirement are ineligible for match.
Ratio of Match:	$2.00 Gov't Match : $1.00 Matchable Private Donations Subject to a grant ceiling for each organization.	$1.00 Gov't Match : $1.00 Matchable Private Donations Plus: $1.00 Gov't Match for each dollar contributed by corporations that have not made a cash contribution to the arts in the previous [illegible] years. Subject to a grant ceiling for each organization.
Total of Gov't Match:	$18 million over three year program.	No figures yet available.
Constraints on Use of "New" Private Money:	Donations over the base must be used for: - Retirement of debt accumulated in a previous year, then - Inclusion into a separate investment (endowment) fund, or - An approved special project extraordinary to normal operating expenses for which a future funding expectation will not be created.	Private donations over the base must be placed in an endowment fund for at least a five-year period. Interest on the endowment is available for operating expenses.
Constraints on Use of Matching Money:	Must be placed into an investment (endowment) fund. Interest income must be available for ongoing operations. Principal must remain in fund for 5 years.	Must be used to retire an existing or accumulated deficit incurred during the [illegible] year participation period or be placed in an endowment fund.
Required Documentation:	Detailed application with audited financial statements and details of proposed fundraising campaign. Strict requirements for documentation of matching grant in organization's future financial statements.	Detailed application with audited financial statements and details of proposed fundraising campaign. Letter from corporation attesting that it is a new donor. Strict requirements for documentation of matching grant in organization's financial statements.
Involvement of Intermediary Institution:	None	None

- DIVERSIFICATION OF SOURCES OF SUPPORT--It is often argued that one of the strengths of American support for the arts is that it involves a diversity of sources making a diversity of decisions concerning what art forms and what art activities are worthy of support. To the extent that matching grants can provide incentives to extra-governmental sources of support, they are seen as important contributors to that diversity.

  Elements of this rationale can clearly be seen in the goals of the three case programs. Yet, in this quest for diversity lies the germ of its demise: a matching grant is designed to make funding sources fall in line with, and parallel one another. Thus, the decisions concerning arts support become dependent rather than independent. Private funding sources, particularly corporations, have been criticized for their unwillingness to exert independent aesthetic judgments and for their over-reliance on the endorsement of the government to trigger private actions.(9) From this perspective matching grants might be seen as a constraint on private decisions, eroding private responsibility and initiative.(10)

- MOVING PRIVATE RESOURCES--If a government determines that a particular sector of the nonprofit economy is receiving too little support, it might design a matching grant to move private resources into the targeted sector through making that use of private resources more attractive by changing the relative prices of the various uses of those resources. To the donor, a credible matching grant can magnify the effect of his or her donation by the matching ratio, making that particular use of money relatively more attractive.(11)

  It is this rationale that is most prevalent in recent matching grant programs, though, understandably, the rhetoric surrounding the programs focuses less on moving private resources around than on increasing them (from the arts organization's point of view). But attracting increased private resources to the arts must have implications elsewhere, perhaps in fewer resources available to other nonprofit activities, perhaps in lower income or profits, or even perhaps in lower contributions to one arts organization, offsetting higher contributions to another.

- DISTRIBUTION OF LIMITED RESOURCES--It is often argued that in an era in which public resources are perceived as limited it becomes particularly important to multiply the effect of those resources, and a matching grant seems a logical mechanism to accomplish that.

- COST SHARING TO INTERNALIZE EXTERNALITIES--Programs that are funded entirely on the local level may be underfunded if they involve positive externalities that are enjoyed by individuals who are not members of the local community. Such an argument has often been made with respect to the funding of arts institutions. In such cases it can be argued that there ought to be cost sharing with a higher level of government that collects its revenues from those taxpayers who are enjoying those externalities. A matching grant is one form that such cost sharing might take. This rationale, however, is more applicable to projects that are begun on the local level and expanded by the match than to projects that are begun on a higher level and sold to local communities.

While all of these rationales may be applied to any matching grant program, cost sharing to internalize externalities suggests a related rationale that applies uniquely to reverse matching grants:

- LIMITING GOVERNMENT DECISIONMAKING/DISCRETION--If a government wishes to decentralize decisionmaking concerning the allocation of public resources, either because governmental decisionmaking is fraught with difficulty (as it is with the aesthetic issues and potential for censorship that government support of the arts entails) or because it wishes, as a matter of policy, to mimic and augment private local decisionmaking (as it would through an education voucher program or, indeed, as it does through tax incentives for charitable donations), a reverse matching grant program in which the public match automatically follows the private decision is attractive.

  This is not to say that all reverse matching grants are constructed from this viewpoint. Neither printed materials nor personal interviews on each of the case studies revealed any explicit discussion of limiting government decisionmaking, even though the Massachusetts program was developed at a time when the state legislature had placed an administrative cap on the Council and the British program was implemented in a policy environment in which no new program that could be administered in the private sector was allowed to be administered in the public sector.

In any particular matching grant program a combination of these motivations is at work, sometimes in an internally contradictory way. It is critical to understand which of these motivations is at work in order to evaluate a particular matching grant program in its own terms.

But it is also important to recognize another, more subtle motivation for the use of matching grants that has more to do with the relationship between the government agency and its funding source than with the relationship between the arts organization and its funding source. Matching grants have not been the centerpiece of any government's funding strategy vis-a-vis the arts. Rather, they represent marginal increases in a government's funding commitment, even in the United States where the overall level of government support for arts organizations is so much lower as a percentage of operating expenditures than it is in other countries. And therein lies a key to understanding the new popularity of matching grants in the arts:

PROPOSITION #1: The important leverage provided by matching grants lies less in the degree to which it leverages new private support than in its ability to leverage new government support for the arts.

In a period of limited resources for government arts support, those government agencies that have proposed matching grants to their legislatures seem to have had greater success in convincing them to increase their budgetary commitment to the arts. Not surprisingly, in all three of the reverse matching grant programs the government's position has been that these matching grants are in addition to the government's normal commitment to the arts; the facts seem to indicate that that is indeed true: The Regional Corporate Challenge Program was designed in response to the Massachusetts Legislature's suggestion that it would only increase the Council's budget if the increment were to be used to leverage further private support; the Wintario Challenge Grant and its successor, Investment in the Arts, were designed to get the Ministry access to otherwise unavailable provincial lottery monies; and the Business Sponsorship Incentive Scheme was the only way that the Minister, Lord Gowrie, claimed he could get additional resources for the arts.

THE PROBLEM WITH "NEW" MONEY

Most matching grants in the arts are designed to provide an incentive to increase the flow of money to the arts by matching "new" contributions. But the concept of "new" money has been a particularly tricky one to operationalize. In most cases it has been taken to include both first time contributions and increased annual contributions, perhaps with a different matching ratio for each (e.g. the Ontario Investment in the Arts program and the British Business Sponsorship Incentive Scheme), but within the concept of increased annual contributions is considerable leeway.

The Massachusetts Regional Corporate Challenge Program began with perhaps the most ambitious definition of new and increased money. It offered to match net increases in the aggregate of corporate cash contributions for general operating support by each Regional Business Committee. A match would be paid only if total corporate contributions to all organizations in the region went up. But while this undoubtedly reflected the original goal of the program, the Council quickly found itself under pressure to move off of this high ground. Some of the Regional Business Committees lobbied successfully to have the Council match net increases by any member of the Regional Business Committee so that businesses whose corporate support dropped would not be counted against those whose aggregate had increased. Then, arts organizations began to lobby the Council, first to match net increases in aggregate corporate contributions made to each organization (so they would not be penalized by decreases on the part of other corporations or to other organizations) and finally to match any increase from any corporate donor. Thus, the original criteria were successively relaxed, each time making the matching program more expensive for the state and less effective in promoting the original goal of increasing aggregate corporate giving. By its third year, the Regional Challenge Program found itself increasing the aggregate matching grant to regions where corporate support had declined.(12)

The concept of new money was relative. To the State "new" money was an increase in the annual aggregate of corporate giving. To each arts organization "new" money was the increase in support that it received from each corporate donor, irrespective of whether that money had been shifted away from another charitable recipient or even away from another arts organization. From the perspective of each corporate donor, new money was, at the very least, the increase in the corporation's total charitable budget for the arts. But for any private donor it is not too difficult to argue cogently that in a new year any contribution is new money, representing a new decision and a new expenditure.

The Ontario programs use yet another method for determining whether a contribution is matchable new or increased money. First, an average fundraising base--the average percentage of operating income raised through private fundraising--is determined for each organization for the years preceding the program. Increases in private fundraising above the amount of fundraising implied by multiplying the base percentage by the year's operating income are matchable.

Whatever definition of new money is used, it is critical that the government agency providing the match (or its designated agent) be able to clearly document that the definition of new money has been met. This requires an agency that is willing to take a firm hand with its clients and insist on rigorous paperwork and documentation. The Ontario Ministry feels it has been able to assure that only new money has been matched because of its requirement for audited multi-year financial statements and its insistence that the matching grant and the matched private funds be accounted for in specified ways. This not only reinforces the definition of new money but is also intended to force the organization to spend both flows of the money according to the requirements of the program. In Great Britain, the Association for Business Sponsorship of the Arts insists on documentation from both the arts organization and the corporate sponsor because both perspectives must be checked to be certain that its definition of new money has been met.

But both of these cases are examples of places where government arts agencies have a long tradition of investigating the fully-audited accounts of their clients because the government is a major provider of direct ongoing operating support to the institution. Where the arts funding tradition has been one of funding projects, as it has been for the most part in the United States, the government agency seems to feel less able to insist on standardized audited accounts. A major difficulty in the Massachusetts program was the lack of standardized documentation procedures across regions and across institutions. At any point in the program it was very difficult to check what definition of new money was being used and whether the flows of money that were being matched actually met that definition.

PROPOSITION #2: Arts organizations and private donors will act to move any program to match new private money toward one which matches increases by individual donors to specific arts organizations, the most desirable outcome from the standpoint of the donor, the most remunerative outcome for the arts organization (in the short run), and the most costly and perhaps least effective outcome from the perspective of the government funding agency.

HOW EFFECTIVE ARE MATCHING GRANTS?

To what extent have increased private resources been induced by matching grants? Any government agency would like to be able to say--and many do--that its matching grant not only elicited the private match its matching ratio would imply but that it had also gone well beyond that ratio. Once the matching money has been spent, government arts agencies will report that their matching grants have been a success and that private donations (or whatever is intended to be matched) must have increased in proportion to the matching ratio. Although the data collected within most matching grant programs are insufficient to document the true extent of matching, the experience with these three matching programs, particularly the Massachusetts one, suggests that extrapolating from the matching ratio may be overly optimistic.

Beyond the fact that successive relaxation of the program criteria led to increasingly expensive matching grants, the evaluation of the Massachusetts Regional Corporate Challenge Program also documented that private donors, with the cooperation, if not the urging, of the recipient arts organizations, gradually adopted a wide range of entrepreneurial responses to the matching grant, maximizing the match while minimizing the cost to corporate contributors:(13)

- REDIRECTION AMONG INSTITUTIONS--Moving a constant contribution around to different eligible arts organizations each year, making the contribution look like new money from the perspective of each new organization. A match can also be triggered by moving a contribution from an ineligible institution to an eligible institution.

- MOVING DONATIONS OVER TIME--A match can be triggered by moving donations forward or backward over time and aggregating them: e.g., a bank that normally gives $500 on an annual basis might be asked to make one contribution of $1,500 to cover the next three years, triggering a $1,000 match without increase aggregate contributions over time.

  A match could also be triggered through cyclical donations. If the donor were to make contributions every other year instead of every year, each contribution would be matched in full because it would look like a new contribution as compared to the previous year.

- REDIRECTION AMONG CORPORATE AFFILIATES--Corporations with a variety of allied entities could move their contributions around internally each year, making them look as though they were coming from new corporate donors and triggering a match. (In Ontario, the private foundations directly affiliated with the major arts organizations moved money into the organizations in the hopes of triggering matches.)

- SUBSTITUTION FOR PRIVATE CONTRIBUTIONS--Perceiving that its support can be provided to the arts at half price (with a 1:1 match) the donor may actually end up giving less than he might otherwise have given. This response to a matching grant means that private money has substituted for public money rather than supplementing it. Across all three programs interviewees said that their fundraisers loved the matching grant because it meant that they only had to raise half of the cost.

  Yet, at the same time there is the contradictory view that the overall result may be the eventual substitution of private resources for public resources and a weakening of the public sector's commitment to the arts. This point of view sees the half-price deal as a deal enjoyed by the government; it is able to buy programmatic initiatives at half-price.

All of these responses can be observed in one or more of the three sample programs. In certain regions of Massachusetts the bulk of the match received can be attributed to these entrepreneurial responses rather than to real increases in private support. Program administrators in Ontario and Great Britain, while recognizing that some such responses have occured, believe that they have been kept to a minimum.

To be sure, the extent to which each response dilutes the overall leveraging effect of each program is a function of the care that was taken in program design and reporting requirements. Without a firm fulcrum a lever cannot work. But these three cases also suggest at least one other possible explanation:

PROPOSITION #3: The more that private philanthropy has matured in a particular country or in a particular region, the less effective a matching grant will be. The closer private contributions already are to their natural limit--whether that limit is economic or cultural--the more likely the matching grant program will fuel entrepreneurial responses.

REVERSE MATCHING GRANTS AND CORPORATE SUPPORT

Many recent matching grant programs have been part of an effort to target increased corporate support. Countries in which private support has historically been small seem to feel that the place to begin seeking private support is where it is easiest to make the case that the arts can provide an identifiable benefit to the donor and that suggests corporate donors who can use the arts to enhance their public image. Even in areas with substantial private support, growth in corporate support is being emphasized. Two of the programs are targeted specifically toward corporate support, and the second phase of the Ontario program rewards corporate support through a higher matching ratio. Is the fact that all three programs also provide reverse matching coincidental? Or can it be linked to the pursuit of corporate support?

To sell a support program on the grounds of benefit to the corporate donor virtually requires that the corporate donor's logic be allowed to lead the program. Where does that donor see the clearest and highest benefit? The match rewards and furthers the donor's choice, rather than trying to shape the donor's choice (beyond moving it into the arts sector). And it provides a government endorsement of sorts for the corporation's activity. The Ontario program was restructured when its administrators realized that corporate donors were not interested in providing endowment support and would prefer seeing their support go to ongoing operations where their support could be associated with identifiable projects (even though projects were not supposed to be matched). Similarly, in Massachusetts considerable pressure was exerted to get corporately funded projects matched.

This logic has been taken to the extreme in the Business Sponsorship Incentive Scheme. Not only is the program limited to matching increased sponsorship, which in British tax law must be demonstrably in the direct interest of the corporate sponsor (as compared to philanthropy), but the public match is to be spent by the arts organization to "enhance" the value of the sponsorship to the corporate sponsor. Some sponsors have taken this even one step further by making those "enhancement" expenditures themselves and then recouping the match from the arts organization when it is received, totally internalizing the benefit to themselves.

Some research has been done on the effect of piggybacking public support on private decisions, though it has focused primarily on the effect of tax incentives (which are themselves reverse matching grants).(14) Research has also been done on the patterns of charitable support, and what clearly emerges is that corporate donors have their own preferences that are not necessarily in accord with articulated public policy vis-a-vis the arts.(15) The effect of these preferences is magnified by reverse matching.

PROPOSITION #4: Designing a matching grant to attract corporate support leads to reversing the traditional logic of matching grants in two ways: by allowing public resources to follow private resources, and by emphzsizing the establishment of a direct, identifiable benefit to the donor more than the financial benefit to the donee.

What is the appropriate role of government in funding the nonprofit sector? Is it appropriate for a public policy to follow and reinforce private decisions, or should it push in specific policy directions? If reverse matching grants become more widely adopted, these questions will become increasingly important.

NOTES

1. National Foundation on the Arts and the Humanities Act of 1965, Public Law 209--89th Congress.

2. Gingold, 1980.

3. The list of reverse matching grant programs for the arts of which I am aware is:
   Massachusetts: Regional Corporate Challenge Program
   Ontario: Wintario Challenge Grant
   Investment in the Arts
   Quebec: Fond d'Appui
   Great Britain: Business Sponsorship Incentive Scheme
   France: Program announced November 1986.

4. I know the Massachusetts program best because I was commissioned to evaluate the program for the state arts council. See Schuster and Perkins, 1986. For the other two programs I conducted a number of interviews with program administrators, donors, and arts organizations, but the level of detail was, of necessity, limited, so many of the issues that I was able to document in the Massachusetts program may also be present in the others but were able to avoid my coarser net of inquiry.

5. These rationales are partially discussed in the literature on fiscal federalism. See, for example, Gramlich, 1976.

6. Kalman, 1985 (p. 19).

7. Netzer, 1978 (pp. 89-93).

8. Gingold, 1980 (pp. 90-91) and Clack, 1979.

9. Lipman, 1983 (p. 8).

10. Joyce, 1984 (pp. 32-33).

11. The word "credible" is important here. Because matching grants have become so popular, many organizations are even suggesting to their donors that they make their donations contingent on the receipt of donations from others. Arts organizations I interviewed pointed out that they create phony matches all the time, hoping to attract more donors. Saturation is bound to come with the overuse of this strategy.

12. Schuster and Perkins, 1986.

13. Schuster and Perkins, 1986.

14. For a presentation of these issues see Feld, O'Hare, and Schuster, 1983; Schuster, 1985b; and Schuster, 1986.

15. Schuster, 1985a and Useem and Kutner, 1986.

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SECTION ELEVEN

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WORKING DRAFT

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THE PUBLIC SECTOR AND THE PRIVATE: ORGANIZATIONAL CHOICE AND THE THIRD SECTOR IN EUROPE

by

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Public Policy and Philanthropy"

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INTRODUCTION

This paper is primarily concerned with the preliminaries of a comparative sociological theory of the third sector. Throughout, the notion of organizational (institutional) choice is used in a broader, historical sense, and refers to the decisions and circumstances which lead organizations to assume either a for-profit, nonprofit or public, governmental form[1]. The paper first discusses the applicability of available theories of the nonprofit sector for comparative purposes. Following this the paper suggests several propositions intended to guide comparative sociological research to focus on the development of "middle-range" theories which either address specific organizational forms (e.g. foundations, private welfare organizations, or advocacy groups) or cover comparable sets of countries.

Critique of available theories

When theories of non-profit organizations were first introduced in the 1970's, they were basically developed with the organizational universe of the United States in mind. Hansmann's contract failure thesis states that, under the condition of information asymmetry, nonprofit firms are more trustworthy than forprofit firms because forprofits have more of an incentive to down-grade product quality. Weisbrod's medium voter theory suggests that nonprofits meet demand not fulfilled by the government which tries to maximize the likelihood of reelection. Hansmann (1987) has discussed the strengths and limitations of both theories when applied to the U.S. organizational universe. Here, we will focus on their applicability to economic, political and cultural settings which may be different from the American experience.

In a comparative perspective, James (1987a) has already pointed out several shortcomings of both the contract failure and the median voter thesis. They neither explain variations in third sector size, nor can they account for the role of religion as the major founder of nonprofits, and the role of the state as the major provider third sector financing. We can add that the notion of information asymmetry appears as an ahistoric concept which ignores the fact that asymmetries are often institutionalized and primary result of non-market social systems. Thus, using the market notion as the sole and central building block in constructing a comparative theory of nonprofit organizations is problematic in as much as (historically) the market has rarely presented a viable and politically feasible alternative in service provision.

More than markets, however, the state, and the public sector at large, appear as alternative choices. In many historically important cases (such the German welfare associations, the Dutch verzuiling, the French étatisme) it was either the state itself or religious entrepreneurs in political alliance with the state, and not nonprofit manager, who made the decision of organizational choice. Conventional theories of the third sector assume a "passive" state — a state which occupies a neutral position between the forprofit and the nonprofit sector, with no influence on the definition on sectoral boundaries, institutional form and organizational choice.

The median voter thesis faces another challenging problem: Service provision to the median voter forms the decisive background variable which helps explain the existence of nonprofits via a second set of variables, differentiated and excess demand. Yet is this orientation of service provision indeed a viable strategy to maximize the probability of re-election? If it were, then governments which, in the course of the last 10 to 15 years, directed their policies at the median voter are expected to have remained in power with greater likelihood than governments whose policies run counter to median voter interests.

It is here that we encounter a paradoxical situation: governments which had been successful in providing public and semi-public goods to the population remained in power as likely as governments with low public policy effectiveness (Schmitt 1983, 14-15). In a study on governmental performance and election results in Japan, Austria, Sweden, Norway, Germany, Italy, Britain and the United States, Schmitt (1983) shows that governments which spent generously on public goods and pursued a successful economic policy were as likely voted out of office as they were able to remain in power. The same pattern prevailed for unsuccessful governments. Startling as these results are, they raise more problems than they answer. However, the important point is that the median voter is either less predictable in his voting behavior than assumed or that other factors play important roles. In any case, in a cross-national perspective, the median voter theory rests on uncertain grounds.

Douglas (1983) and, in particular, James (1987a,b) were the first to present comparative theories. Douglas' basic thesis, an extension of Weisbrod's theory, is based on the free rider problem. The theory assumes that the state has to serve all of its constituencies. Therefore, it is categorically constrained in its spending pattern and flexibility. Nonprofits, not facing the state's categorical constraint, combine the flexibility of markets with the production of public and semi-public goods (Douglas, 1983: 116).

An important limitation of the categorical constraint thesis is that it fits countries with a relatively stable and established state apparatus in a liberal market economy best. While the categorical constraint may apply to the U.S. and Britain, it can much less convincingly explain variations in size, composition and importance of the nonprofit sector. Moreover, the categorical constraint thesis finds it difficult to take account of variations in the welfare state cross-nationally[2] .

James (1987a,b) adds a welcome inductive flavor to theory construction, and combines the virtue of informed conceptualization with empirical evidence from a diverse set of countries. She hypothesizes a strong and positive relationship between a society's religious heterogeneity and the size and importance of its third sector. Heterogeneous countries such as the Netherlands develop a large third sector, while homogeneous countries like Sweden are characterized by a small third sector. While differentiated demand for services such as education explains the differential size of nonprofit sectors in developed countries, excess demand for services combined with donor preferences and religious competition among suppliers explains differences in the third world (James, 1987a).

James' heterogeneity thesis tends to neglect historical factors, in particular the historical influence of political power on organizational choice (see below). First, large segments of the third sector in (most) European countries are a product of political conflict between secular and religious power. Second, the state must allow heterogeneity to manifest itself in organizational choices. However, often heterogeneity, social inequality and power differential are closely related. Thus, the presence of heterogeneity does not necessarily imply the manifest expression of heterogeneous demand. Third, heterogeneity itself needs further clarification. Religious, ethnic and linguistic heterogeneity are inseparable and highly correlated in some societies, yet uncorrelated and attributable to different segments in others. At present, support of the heterogeneity thesis, is based on cross-sectional analysis and, in one case, on regression estimates for two points in time (10 year interval) (James 1987b). Clearly, the absence of longitudinal data, not theoretical shortcoming per se, constraint the full exploration of the heterogeneity thesis.

Of course, accusing economic theories of treating "state" and "politics", "organizational inertia", "stratification" and "power" as exogenous is as easily argued by sociologists as it is dismissed by economists. In terms of theory construction, however, it has to be shown that sociological criticism matters and may indeed help the conceptualization of a model which can then be tested empirically. To this end, the remainder of this paper will explore several major themes in the form of propositions.

In summary, the paper suggests that in a comparative perspective, theories of the third sector are somewhat biased toward the notion of a liberal state within a market economy, and assume a greater availability of organizational choices (private for-profit, private non-profit, public) than has been the case historically. Moreover, the basic third sector organizations (philanthropic and operating foundations, large-scale welfare organizations, interest and advocacy groups, and local associations) may have evolved independently historically, and responded to rather different social and political circumstances.

EIGHT PROPOSITIONS

1. REASONS LEADING TO THE CREATION OF ORGANIZATIONS ARE OFTEN DIFFERENT FROM THE RATIONALES OF THEIR CONTINUED EXISTENCE.

We need theories which explain not only the reasons why nonprofit firms are created but also why they continue to exist as third sector organizations. This question is related to an additional, though often overlooked, characteristic of the third sector which may have implications for a comparative theory: the relative durability and permanency of core third sector organizations. In many cases, the innovative capacity and flexibility of third sector organizations coexists with their remarkable longevity. Few organizations in Europe are older than some of its foundations, and few more stable than organizations linked to the Catholic Church.

While there are no comparative studies investigating differential organizational life expectancy, we can assume that religious organizations and also foundations have low mortality rates and represent some of the oldest existing organizations. However, in a recent essay Karl and Katz (1987) remind us to differentiate clearly between philanthropic motive and its organizational form. The motives that lead Ford, Carnegie or Rockefeller to establish foundations are different from their raison d'etre and organizational objectives today. Similarly, Poggi (1967) suggests that the reasons which led to the formation of the laity movement in Italy are different from those that are responsible its continued growth. He argues that laity organizations were first "promoted by the church in an effort to establish and maintain viable contact with an estranged world" (Poggi, 1967 p. 52). The laity organizations, once established, were not easily treated as instruments of church policy only, and they began a search for goals different from the ones that led to their creation.

Nineteenth century Germany offers a prime example for the important difference between motive and organizational rationale. When Bismarck laid the foundation to a more comprehensive welfare system he did so for political reasons and against the opposition of established religions. Social insurance and welfare was used as a tool of social and political control (Rimlinger 1971, p.114); social rights to welfare were granted, in part, to prevent the transfer of greater political rights. The decidedly political nature of the origin of the welfare state cannot be overstated. Traditional support system (family, church, charity) had proven inadequate to meet working class demands. This "has not been a minor factor in inducing members of this class to seek the road to relief by supporting Social Democratic aims" (William I, Opening address to the Reichstag 1881, translation quoted in Rimlinger 1971, p. 113).

Likewise, the conflict between Bismarck and the Catholic Church (Kulturkampf) between 1871 and 1891 was, to a large extent, a political conflict between secular and religious powers over the division of labor as well as influence and responsibility in the areas of education, culture and welfare. The outcome, ultimately based on power differentials rather than means-rational, market or efficiency considerations, influenced and continues to influence the development of Germany's entire third sector. Even during the Weimar Republic (1920-1933) the ministries of welfare remained in the hands of the Catholic center parties. This historical development resulted in the typical corporatist pattern of the German welfare system (see below). The long term consequences of historical choices lead to the second proposition.

2. HISTORICAL CONTINGENCIES ARE MORE IMPORTANT IN THE THIRD SECTOR THAN IN MARKET SYSTEMS.

In a recent paper, Seibel (1987) suggested that the nonprofit sector offers an arena for dealing with problems that have been rejected by both public and forprofit sector. He argues that, for various reasons, politicians delegate "unsolvable problems" to the third sector. The nonprofit sector is certainly more than a dumping ground for unsolved and unsolvable problems, yet most European countries have utilized the third sector alternative. It is useful to think of the governmental use of the nonprofit form as an attempt to build a "buffer" between the public and the private.

There are various forms of such "buffer" organizations (Hood, 1984:9; Rosas, 1984; Himmelmann, 1985) which range from independent public associations to public foundations and quasi-non-governmental (Quango) organizations. They allow the state to delegate public matters to specialized agencies. In countries with a well developed tradition of indirect public administration (e.g. West Germany, Austria, Switzerland), Quangos have tended to increase in numbers, and subsequently formed an imperium in imperio (Hood, 1984) which now transcends both private and public spheres.

We can also make the more general case and argue that third sector organizations are less subject to selection processes and pressures than both public and forprofit sector. The third sector has only partial access to a mechanisms of correction comparable to that of the market in the case of the forprofit sector and that of the ballot box for the public sector. As a consequence, historical contingencies show longer-lasting effects and are perhaps of greater importance in the third sector than in both the public and the forprofit sector.

Finally, two examples show the influence of exogenous factors on the creation of two of Europe's largest foundations. The Volkswagen Foundation (Stiftung Volkswagenwerk), established in 1961, is the result of a complex settlement of a lengthy legal dispute concerning the ownership of the state-owned Volkswagen corporation in 1945. A less dramatic example is offered by the Calouste Gulbenkian Foundation. The foundation was established in 1956 Portugal. However, apart from the personal preferences of it founder, Mr. Gulbenkian, to live in Lisbon, it is difficult to think of social, political or economic variables which help explain why one of the world's largest foundations happens to be part of Portugal's third sector, or why a third sector traditionally dominated by Catholic organizations contains a comparatively large secular foundation.

3. THE "PUBLIC" AND THE "PRIVATE" ARE NEITHER DICHOTOMOUS NOR DOES MORE PRIVATE NECESSARILY IMPLY LESS PUBLIC AND VICE VERSA.

Sociologists have long argued that "public" and "private" are neither constant concepts nor a zero-sum combination. Even "core" third sector organizations receive differential legal and political treatment cross-nationally along the public-private dimension. Rosas (1984) has shown that the classification of National Red Cross Societies ranges from "public associations" and "noncommercial membership organizations" regulated under private law, to "mass voluntary public organizations" governed by public law.

The division of responsibility between private and public sectors is, as Kramer (1981) suggested, neither stable nor formalized. An example from the Bavarian foundation sector demonstrates the complex overlap between public and private sectors in terms of social and legal differentiation. Overall, there are about 40,000 catholic and 15,000 protestant church foundations in West Germany, as opposed to about the 4,500 "secular" foundations outside the arena of ecclesiastic law (see below). The church foundations are regulated by ecclesiastic law, which is constitutionally equivalent to public administrative law. Moreover, in Bavaria, the 1,500 protestant church foundations form a federation organized under public law (Körperschaft des öffentlichen Rechts). Thus, three legal systems meet in a complex interaction, each classifying and treating the same organization somewhat differently.

4. DIFFERENT SEGMENTS OF THE THIRD SECTOR HAVE DISTINCT HISTORIES AND ARE THE RESULT OF DIFFERENT POLITICAL AND ECONOMIC CIRCUMSTANCES.

Far from being a uniform sector, third sector organizations can be organized and constituted rather differently. Some third sector organizations, which began as small welfare organizations and independent charities, emerge as giant health insurance schemes (such as the German Krankenkassen); others, which began mutual assistance organizations among local farmers develop into multinational nonprofit corporations, such as the Raiffeisen group. The basic third sector organizations may not at all together reflect a common theme in a particular country; rather, they may have evolved independently historically, and responded to rather different social circumstances.

For example, the history of Italy's third sector (Ponzanelli, 1985; Pasquinelli, 1987) shows that foundations, large-scale charities, and local initiatives entail three different "stories." All are, however, related to the major conflictual ingredients of Italy's complex history: the political philosophy of state intervention and centralization, the semi-official character of the Catholic Church, and strong desires for local or regional independence.

In Italy, charities in the fields of health and general welfare used to be quasi-official church organizations. The Catholic welfare system (Opere Pie) was legally and financially autonomous from the state. In the middle of the 19th century, some 20,000 institutions were run by Opere Pie. In 1890, against heavy opposition by the church, the state introduced the beginnings of a public welfare system. During the Fascist period (1922-1940) and after World war II, state and church were in more or less constant conflict over the welfare system (Filtzinger, 1987). In 1977, charities were put largely under municipal control. The school system, with the exception of higher education, is the domain of both public and private (mostly Catholic) schools. Foundations remain few in number and are outweighed by direct corporate philanthropic activities. Local initiatives have a much longer history, many of which received new impetus through the decentralization policies of the 1970's (Pasquinelli, 1987). Thus, for the last century, Italy's third sector has been constantly revised and reorganized, with each revision and reorganization reflecting the political power constellation at that time.

The German foundation sector also demonstrates that various segments of the third sector are the product of different historical conditions. The German foundation sector has been subject to severe discontinuities during the last century, in particular the political turmoil following WW I, the economic collapse of the early 1920's, and the Nazi-Period, when all foundation matters were extremely curtailed. Although the oldest German foundation dates back to the year 917 (the Hospitals-Stiftung), about 40% of the some 4,500 foundations in the country were founded after 1960[3]. 15% were created in the first post WW II decade, between 1951 and 1959; and another 15% during the Weimar Republic in the 1920's. About 20% were created in the 19th century; 10% between the 16th and 18th century, with about 100 foundations predating the year 1500. During the 1970's about 60 new foundations were created while between 30 to 50 were dissolved each year. In the early 1980's there has been an increase in the birth rate of foundations: 131 were established in 1983 and 120 in 1984, with only 36 terminations in the course of the two years.

5. ORGANIZED RELIGION, ONE OF THE MOST IMPORTANT VARIABLES IN EXPLAINING VARIATIONS IN THIRD SECTOR SIZE, COMPOSITION AND IMPORTANCE, PLAYS A RADICALLY DIFFERENT ROLE DEPENDING ON BOTH THE TYPE AND THE DEGREE OF STATE-CHURCH SEPARATION.

One particular characteristic (which applies foremost to larger welfare, social service organizations, but also to some foundations and local associations) is important to understand the development of the third sector in several European countries: they are often based on strong ideological components, and religious rather than secular in their value-orientation, and, following the Weberian distinction, value-rational rather than means-rational. The value rationality or, following Bauer (1987), *Weltanschaulichkeit* of third sector organizations, implies a deeply rooted set of values, a reservoir of philosophical and religious convictions, which motivate and guide the organization.

The most conspicuous examples of *Weltanschaulichkeit* are the religious entrepreneurs of the 19th and 20th century. Johann Hinrich Wichern, founder of the influential *Innere Mission* saw his organization as the "armed daughter of the church" (in a speech presented to a congregation at Luther's church in Wittenberg) against communism and atheism (Heinze and Olk, 1981). Similarly, Wertmann (the founder of CARITAS), Bodelschwingh, Bethel, Booth and Dunant are other examples of religious entrepreneurship, some of which even founded family dynasties.

The "free welfare associations" in West Germany are a case in point. Their corporatist arrangement is closely related to the *Weltanschaulichkeit* of the third sector. The five free welfare associations[4] were founded in the 19th and early 20th century. Organized in a "peak" association at the federal level they represent a net worth DM70 billion and run more than 60,000 institutions in the area of health care, youth and family services, as well as services for the handicapped, elderly, and the poor[5]. An additional 22,120 self-help groups, clubs and local voluntary associations enjoy associate status. They provide 70% of all family services, 60% of all services for the elderly, 40% of all hospital beds, and 90% of all employment for the handicapped. The free welfare associations employ nearly 500,000 full-time and about 175,000 part-time staff. The number of volunteers is estimated to range between 1.5 and 2 million. *CARITAS* alone employs more people than the industrial conglomerate Siemens, one of the largest employers in the Federal Republic.

It is important to note that the free welfare associations are not at all the result of purposive collective decisions to provide welfare and to cater for the public good. Most of the associations originated primarily for political reasons; the legal and social policy rationales of the system were introduced afterwards. They did not primarily develop in response to consumer demands, but are largely unintended consequences of sometimes accidental policy decisions (Bauer and Dießenbacher, 1984; Sachse and Tennstedt, 1981).

6. THE THIRD SECTOR ACCOMMODATES AND PRODUCES HETEROGENEITY.

In several European countries, corporatism presents a major aspect of the third sector. There are many different versions of corporatism (Williamson, 1985; Streeck and Schmitter, 1985), ranging from liberal to authoritarian forms. It has a long history in several European countries such as Switzerland, Austria (Katzenstein, 1984) and West Germany. Today's contract corporatism in central Europe originated from the consensual-licenced corporatism of the late 19th century. 19th century corporatism was a reaction against liberalism rather than capitalism, and sought to reconcile religion with the new economic and political conditions (see the papal encyclical Rerum Novarum of 1891 and Quadragesimo Anno of 1931 which formulate and advocate the principle of subsidiarity).

Today, central European corporatism is the acknowledgement and channeling of deep-seated societal conflict (such as religious or labor - management conflicts) by "peak" associations. These peak associations then negotiate policy issues on the basis of cooperation and coordination, seeking a common solution. The strength of corporatism, regulation of divisive conflicts, is at the same time its major weakness. Corporatism has been criticized as an arrangement which preserves rather than overcomes conflict (Thränhardt, 1983).

While corporatist arrangements accommodate heterogeneity, other parts of the third sector produce it. The political party foundations, one of the characteristic features of Germany's foundation sector, are, with the exception of the social democratic Friedrich-Ebert-Foundation (created in 1925), a product of the 1950's when the British and American powers tried to encourage the development of democratic parties and trade unions. Today, the political foundations operate on an international level. It is important to note that the political foundations are not a product of differentiated taste and heterogeneity but their producers. Beyond the special case of the political foundations, it can be argued that third sector organizations "are much more than passive recipients of preferences put forward by their constituents and clients" (Streeck and Schmitter, 1985: 19); third sector organizations are also producers of interests, tastes and preferences, in other words: heterogeneity.

7. THE TYPE OF REGULATORY REGIME INFLUENCES THE ORIENTATION OF THE THIRD SECTOR.

To take account of the political context of the third sector, it is useful to differentiate third sector along three dimensions. First, we distinguish three regulatory regimes. The liberal and the conservative regulatory regime reach back to 19th century, while the social democratic regime is essentially a 20th century, post world war II product. The second dimension, religious homogeneity/ heterogeneity refers to either a Catholic or Protestant hegemony or whether the population is religiously heterogeneous. The third dimension is the degree of centralization-decentralization of public service delivery or welfare state activities. Equipped with these three dimension, it is possible to a) identify and examine groups of countries with comparable attributes, and b) investigate distinct third sector forms (such as foundations) across different cells.

For example, with the first two variables at hand, we can construct the simple typology. Table 1 shows "pure" types, such as the liberal-protestant combination with the United Kingdom as the prime example, or the Catholic-conservative combination in the case of Austria, France and Italy. Table 1 also shows certain deviations such as Ireland (Catholic-Liberal), the Netherlands (mixed-liberal), and Germany (mixed-conservative).

Table 1: Regulatory Regimes and Religious Heterogeneity

Religion	Regulatory Regime		
	Liberal	Conservative	Social Democratic
Protestant	U.K.	(?)	Sweden Norway Denmark Finland
Catholic	Ireland	Austria France Italy	(?)
Mixed	Netherlands	Germany	(?)

State-oriented third sector. Civil law countries, exemplified by France, Germany, Austria and Italy, are rooted in a mixture of etatist (later corporatist) reformism and Catholicism. With the exception of France, they are countries where the church played a dominant role in the social reforms following the industrial revolution and where absolutism was comparatively slowly or incompletely abolished. Although to some degree dependent on the degree of centralization, civil law countries developed a state-oriented third sector. Organizations in the third sector tend to resemble the state agency more closely than the for-profit firm. As part of the sector's self-understanding and characteristic, public service provision is emphasized over voluntarism.

In France, the absence of both state church and aristocracy after the revolution, combined with a strong republican or centralized state tradition produced a weak third sector in the past. Given that country's historical tradition of a relatively centralized state, where "private" initiatives in "public" domains were guarded with great suspicion by the central state, the new association movement is closely related to the decentralization of political power and administration. To a large extent, the decentralization has led to a renegotiation of power at local levels (e.g. Triomphe and Caye, 1982; Ferrand-Bechmann, 1982; Archambault, 1985). Today, France accounts for about 500,000 associations with 20 million members, 780,000 employees, and 600,000 volunteers (Férrand-Bechmann and Murswieck, 1987). Férrand-Bechmann and Murswieck also report that the number of new third sector organizations increased from 13,000 in the year 1960 to 47,000 in 1983.

Market-oriented third sector. In common law countries, the third sector is more market-oriented. It puts more emphasis on voluntarism than the public weal, and nonprofit firms tend to resemble the forprofit firm more than the state agency. The liberal third sector originated with the English Poor Law of 1601 and is today found in such countries as the United Kingdom, the U.S., Canada and Australia. While in common law countries the state, for political reasons, tried to incorporate social welfare into state affairs, the liberal state tried to restrict involvement in welfare activities.

8. HOW SOCIETIES DEFINE PRIVATE, SEMI-PUBLIC AND PUBLIC GOODS HAS CONSEQUENCES FOR THE SIZE AND IMPORTANCE OF THE THIRD SECTOR, AND ALSO FOR THE PUBLIC SECTOR-THIRD SECTOR DIVISION OF LABOR.

A special case falling outside the "conservative" civil law countries and the "liberal" common law countries are the social democracies of Scandinavia. They demonstrate that the political definition of goods clearly influences the size and the importance of the third sector.

Following Esping-Anderson (1985), four characteristics of the social democratic regime are important for our purposes. First the state's attempt to "decommodify labor", to exclude labor from the market or, at least, to isolate labor from market considerations. Second, the consumption of basic social services and semi-public goods (education, health) is not distributed via the market, but through a state bureaucracy and turned into a consumer right. Third, a redistribution and restructuring of the economy on the basis of "solidarity", i.e. a policy which favors low income groups. Finally, related to the first characteristic, social democratic regimes try to institutionalize full employment. In particular the institutionalization of solidarity, which replaces both the principle of subsidiarity and the notion of voluntarism in charity, in addition to the change from a "good" to a "right" in the case of basic social services, both necessitate greater state involvement. As a result, the third sector is less developed and less important than in other European countries. In Sweden, for example, there are only 6 private nonprofit hospitals (Elmér 1987).

In summary, in a comparative perspective, third sectors vary substantially along legal and political dimensions. A country's third sector reflects a "distinctive history and sociopolitical context" (Kramer, 1981:4). In a sense, an analysis of the evolution and current state of the third sector tells the history of the country, and way in which societies "chose" to govern themselves.

Notes

1. In fact, the notion of organizational choice is somewhat misleading, since, as the paper argues below, organization often have little choice and decision are made for them.

2. Indeed, one of the important tasks for a comparative theory of the third sector is to examine the applicability of theories of the welfare state and public policy in political science.

3. Data reported in this paragraph are from Soergel and Neuhoff (1978) and Neuhoff, Schindler & Zwingmann (1983).

4. These are 1. Diakonisches Werk (Protestant); 2. German Red Cross; CARITAS (Catholic); 3. Arbeiterwohlfahrt (Workers' welfare, secular and historically linked to the social democratic party); 4. Zentralwohlfahrtsstelle der Juden in Deutschland (Jewish), and 5. Deutscher Paritätischer Wohlfahrtsverband (non-denominational, non-partisan). In the 1920's the communist party ran its own charity organization, the Rote Hilfe (Red Help).

5. Data reported in this paragraph are from Bauer (1985) and Bundes AG der Freien Wohlfahrtspflege (1985). On the history and critical assessments of the free welfare organizations see Sachse and Tennstedt (1981, 1986), Heinze and Olk (1981), Bauer (1985), Bauer and Dießenbacher (1984).

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WORKING DRAFT

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THE ROLE OF NONPROFITS IN A SOCIAL-DEMOCRATIC STATE: THE RELATIONSHIP BETWEEN THE STATE AND PRIVATE ORGANIZATIONS IN NORWAY

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BACKGROUND INFORMATION

In the following I want to discuss the dilemma of dependency affecting the relationship between the state and private nonprofit organizations in Norway. To a certain extent it may be justified to ask whether there is a trend towards turning NPOs into some kind of quasi-governmental agencies. My perspective will underline that of James: To understand the role of NPOs a country in Norway, it is more important to focus on the relationship between government and NPOs than on the comparative advantages of NPOs vs. profit-maximizing organizations.[1] To a large extent the practical (vs. ideological) roots of the problem seem to be found in the economic dependency of the NPOs on the government.

To begin with, some background information will probably be needed:[2] Norway has a population of 4.2 million people. On the average, every Norwegian has two memberships in nonprofit organizations. Only one third of all Norwegians are not members of any organization. There are at least 1,200 national and regional organizations. Since World War II, Norway has been governed by a social democratic government for more than 30 out of 42 years. Legislation affecting nonprofit organizations, especially the tax system and regulatory legislation such as labor law, is highly influenced by social democratic ideology. Norwegian law can hardly be categorized as either common law or civil law, but is influenced by both, like the other Scandinavian legal systems.

Norwegian statistics and research on NPOs are sketchy and unsatisfactory. The NPOs' part of GDP has not been estimated. However, it has been calculated that in 1987 the NPOs received approx. 6 billion Norwegian Kroner (1 USD = 6.40 NOK) in direct and indirect subsidies in 1987. GDP being approx. 560 billion NOK, the "subsidy part" of the NPO-sector may be 1.1 percent of GDP.[3]

FINANCING: THE NET TRANSFERENCE CONCEPT

An important aspect of the Norwegian social democratic state is the high proportion of taxes in relation to GDP; for 1987 estimated to 47.4 per cent. For many years, Norway has been among the three most heavily taxed countries in the world. One consequence for the NPOs has been recognized for a long time: Being subject to high and progressive tax rates on relatively modest income (in 1987 67.4 per cent at approx. 210.000 NOK - USD 33.000), private individuals cannot afford donations of any considerable amount. Consequently, NPOs are not able to rely heavily on private philanthropy. Contributions to NPOs are deductible for scientific and certain educational purposes only.[4]

Another point is more subtle and has only recently been pointed out in the debate: In order to finance the welfare state, it has been necessary to rely more and more on indirect taxation, i.e. VAT, and social security fees. In Norway, NPOs are often called "tax-exempt institutions" as they are not subject to income and wealth taxation. However, this term may be grossly misleading, as NPOs are subject to indirect taxation and have to pay payroll taxes for their employees.

An example to illustrate the above mentioned: The most recent supreme court decision on the income taxability of NPOs concerned a correspondence school.[5] The disputed amount was NOK 110,000 in due income taxes for the year in question. However, the accounts showed that the organization had incurred NOK 53 million in expenses the same year. With the Norwegian VAT at 20 per cent and payroll taxes at (then) 16.8 per cent (1988: 17.3 per cent), it is a moderate guess that the school had paid at least NOK 5 mill., perhaps NOK 7.5 mill., in such taxes. In other words, VAT and payroll taxes had probably amounted to 50-75 times as much as the disputed income tax. The proportion of possibly exempt income taxes to actually paid indirect taxes and payroll taxes may be fairly typical. As most other NPOs, Norwegian NPOs are generally run at very marginal - if any - profits, considering the amount of VAT and payroll taxes due.

Many Norwegian NPOs receive some kind of subsidies from the government. These transferences are often referred to as subsidies without any kind of qualification. However, it could be maintained that there is no net subsidy until the support exceeds the amount paid by the organization in indirect taxes and payroll taxes. In a theoretical inquiry it has - with some empirical basis - been found that most Norwegian NPOs pay at least 15 percent of their total outlays in indirect taxes and payroll taxes. - As a short, more detailed illustration: VAT amounts to 16.68 percent of the total expenses subject to VAT. Payroll taxes amount to at least 14.8 percent of the total personnell costs. In an organisation where 50 per cent of all costs are actually personnell costs and 70 per cent of other costs are subject to VAT, these taxes alone will at least amount to 13 per cent of the total costs.

The concept of net transference naturally has its logical problems. One may, in effect, apply the same concept to physical persons, i.e. for-profit organizations and municipalities. However, the fact that an NPO receives any kind of subsidies, is often used as an argument in favour of governmental control or influence. The perspective of "returning" to the

NPO, instead of just "subsidizing", may indicate the complexity of the relationship between the NPOs and the state. Furthermore, as the organizations are in effect taxed, they may inevitably have some dependence on the state for financing. And the concept of net transference indicates that the growing use of indirect taxation and social security taxes in Norway may emphasize the necessity of a thorough discussion of how the government wants these taxes to influence the growth - or stagnation - of the NPO sector.

INDIRECT SUBSIDIES OR ADJUSTMENTS: PARADOXES OF VAT

In international tax literature - much based on the US pioneering studies - there has been an extensive discussion as to whether exemptions for NPOs represent subsidies, or a logical definition of the tax base.[7] In my opinion, the discussion often presupposes a too clear either-or dichotomy. This may seem very logical and consistent regarding economic theorizing and legal decision-making by courts and administrative bodies. Although I cannot go any further into the discussion here; when it comes to tax legislation, taxes have a much more practical character, often appearing as compromises and both-and solutions.

In the Norwegian debate, it has - inspired by the imported terms "The Third Sector" - been pointed out that the NPOs constitute a part of society different from the government and the market. By going through the preparatory works for legislation on indirect taxation, it has been shown that the legislator has not at all - or only very superficially - discussed whether, to what extent, and how this legislation should be applied to organizations in the third sector.[8] It is far too simple just to state that e.g. the VAT should tax all forms of "consumption", and therefore the NPOs should be included, as they either consume themselves or provide consumption for other consumers. Like any tax system, the VAT is a technical system, which may have paradoxical effects when applied to subjects different from the typical targets of the tax. Adjusting for such inconsistencies is not - as a matter of logic - simply exemptions and subsidies. Furthermore, when introducing an indirect tax which is also to be applied to The Third Sector, it may be inquired whether there should be a discussion as to why NPOs should bear a higher tax burden than before, and if this should be compensated in any way.

In the following, I shall be pointing out some of the problems related to the Norwegian VAT legislation as applied to NPOs. In the present legislation there are only a few minor exemptions for NPOs. A rather small matter seen in an international perspective is the minimum registration threshold in the VAT system, which is very low: a total turnover of NOK 12,000 (USD 1,800) during one year. The reporting and accounting requirements are very demanding (filing six times a year). Any kind of "subsidy" argument is inadequate in describing the rationale behind a possible increase of such registration requirements for NPOs. Referring to "administrative" reasons - a standard, and sometimes vague, - point of reference in tax expenditure discussions, do not clearly point out the special problems relating to NPOs.

The VAT on the sales of NPOs may result in taxing donations. Many sales by Norwegian NPOs will be part of fund-raising campaigns. Such campaigns may still be regarded as sales which are subject to VAT. The only exemption is when the difference between the price and the sales value is so great, e.g. 1:25,* that the thing given most properly is defined as a receipt or a token to prove that a sacrifice and action of support has taken place. But in somewhat less extreme cases VAT has to be paid even though it is quite clear that the transaction basically is a gift, the objects are mostly bought by supporters and there is no real competition with ordinary business. In such instances, the value added by the NPO is also extraordinarily high, with the result that the VAT will decrease the net donation more than is the case in ordinary business, where the profit margin is usually smaller. It has not been possible to find any positive reasoning why there should be such a VAT on donations, except the negative: Exemptions distort the general character of the VAT.

There is also a "40 percent-", and "60 percent-" paradoxical "effect" of the VAT when applied to NPOs, which illustrates that the VAT has not been adjusted to the Third Sector. An example: An NPO erects a building for its non profit purposes. The cost of the building excluding VAT is NOK 800.000. Also NPOs have to pay "incoming" VAT at the standard rate of 20 per cent on purchases, which makes the cost for the organisation NOK 960,000. If the NPO arranges a sale in order to finance the cost of the building, the goods sold will most likely be liable to VAT. To cover the construction costs of NOK 960,000 incl. VAT, the organization has to charge a total of NOK 1,152,000 including VAT for its sales. The VAT paid for the building may not be deducted against the VAT charged on the sales, as the use of the building is to be for non profit purposes and is not connected with the sales in any relevant VAT-sense. The result is that the organization - due to VAT - has to raise NOK 352,000 in addition to the the cost of NOK 800,000 for the building excl. VAT, i.e. an additional 44 per cent.

The problem is extrapolated in cases where the objects sold by the organization are donated by a VAT-registered business. In such cases the donator has to pay 20 per cent VAT on the removal of the goods from his business. Still the NPO has to pay 20 per cent VAT when selling the goods, and 20 per cent VAT on the construction costs of the building, without any of the VAT-payments being allowed to be deducted against each other. Given the numbers in the illustration above, a total of NOK 544,000 now has to be paid in VAT by the business donating the goods and the NPO in order to finance the "basic" costs of the building of NOK 800,000, i.e. an additional 68 per cent.

It is, of course, always possible to point out paradoxical, "technical" effects of tax legislation. But the effects shown above illustrate how the NPOs may easily be subject to unforeseen VAT-consequence. They are partly viewed as consumers and outside the VAT-territory, and therefore subject to pay VAT on purchases without deductibility against the VAT they have to charge when they operate within the VAT-system, e.g. as vendors of goods. - My main conclusion here is that the NPOs constitute a certain - third sector- with their own distinctive VAT-problems. If one, to mitigate such effects, find certain special rules necessary, it is not necessarily appropriate to label them "indirect subsidies". On the other hand, if the legislator, as in Norway, does not implement adjustments to rectify such consequences as pointed out above, it should not come as a surprise that the NPOs will find it increasingly difficult to finance their own activities. By and by they will become more dependent on the government for subsidies ("refunds").

NO INDEPENDENT SOURCES OF FINANCING - LOTTERIES?

In a social democratic state like Norway - not allowing any substantial private contributions to NPOs because of the tax system, and subjecting the NPOs also to indirect taxation - there may be a question of monopolizing certain sources of revenue for the NPOs. The Norwegian Lottery Act of 1939 art. 4 states that permission to arrange a lottery may only be granted for humanitarian and charitable purposes. In other words, there is not to be any competition for this kind of income between the private for-profit and the non-profit sectors. However, NPOs are not allowed to arrange lotteries with cash prizes. The state has granted itself a monopoly of cash prize lotteries, and greatly expanded those during the last years. In 1986 nationwide private lotteries reached total estimated sales revenues of some hundred million NOK, while the state lotteries made a total of NOK 4,547 mill. It may be added that as a kind of compromise between the interests of the state and the NPOs in revenues from lotteries, some part of the state lottery revenue is allocated to NPOs, especially sports organizations.

However, this ratio is gradually diminishing, compared to the marked increase in the total revenues from state lotteries. Again, this development illustrates that the NPOs in Norway are more in a position of "competing" with the government, rather than with the private for-profit sector. Furthermore, the financing of NPOs has been increasingly mixed with the economy of the state.

CONSEQUENCES OF ECONOMIC DEPENDENCY

The widespread subsidizing of NPOs by the government has raised many issues related to the theme of "public influence" on the way "public money" (i.e. direct subsidies) are spent.

Public authorities, often on a regional level, have the responsibility of furnishing the necessary medical services. Various health acts require that these authorities work out plans about how these requirements are to be met. Medical institutions and hospitals run by NPOs may be allowed into the plan. Only then may they receive public support, which in most instances will be an absolute prerequisite for sustaining the institution. The subsidies may reach 100 per cent of operating costs. As part of the regional health plan, the NPO-institution will basically have to submit to the same regulations as state hospitals etc. The difference between a hospital run by the government and one run by a NPO may be very small.

Regarding kindergartens and educational institutions, the consequences of varying levels of direct subisidies have been publicly appointed members of the board, and public influence on admission procedures, curriculum and appointment of employees etc. The influence varies, and may seem to be subject to constant controversy, as it directly concerns the issue of how independent NPOs should be allowed to become. Sometimes the discussion directly involves issues of basic human rights. Norway,- a widely extensive and sparsely populated country, - there are in some places only one kindergarten to be found within a reasonable geographical reach. Christian parents may insist, as their basic parental right, that their children should have access to a kindergarten of their congregation. Non-Christians, or parents belonging to other denominations, may object that channelling public support to one particular nursery makes it impractical and virtually impossible to establish another nursery at the same location, maintaining that they are thus refused their basic right to religious freedom for their children. The debate illustrates the difficulties of basing mainly on public subsidies the financing of an "indpendent" sector which should stimulate plurality and take care of the interests of minorities.

In some instances, a condition for public support may be that the receiving organisation is "democratically" organized (i.e. one man, one vote) and that membership is "open" to anybody, at least anybody satisfying certain objective criteria.[10] Of course, it makes good sense to argue that public money should only be channelled in ways that makes it possible for anybody to benefit and influence. On the other hand, how can minorities or specialized groups rest assured that they may cultivate their own institutions when, in principle, the "majority outside" may always enter and become the "majority inside"?

Another consequence of the "public money" point of view is procedural. The Administrative Act 1967 establishes a broad set of rules of procedure to which public agencies should adhere. Thereby, it is ensured that the power executed by public agencies on behalf of the people should be enforced in a way that take care of the basic rights of the citizens. The reasoning regarding NPOs receiving public support is quite logical and has already, concerning some basic rules of procedure, been regarded by some authorities to have gained the statute of law: Why should NPOs be "exempt" from the same requirements taking care of the rights of citizens (i.e. their members and interested parties) to just and thorough procedures, when the NPOs - just like public agencies - are only able to exist because of public money, i.e. "the money of the taxpayers". The result may be NPOs as quasi-administrative agencies. Again, if NPOs should constitute an independent and flexible sector, there would be a discrepancy. Also, the line of reasoning is interesting. First, it is argued that in Norway "everybody" - also NPOs should pay indirect taxes. Then the NPOs have to adjust their behavior, organizational structure etc, because - since they receive public subsidies - they administer the taxpayers' money. At least until the NPO in question receives a net transference, see supra, this line of reasoning does not seem to hold. More vitally, it resuires a more basic discussion as to what kind of independence is necessary for the third sector to fulfill its functions..

When NPOs receive public support, it is easy to start thinking of them as tools for the government. One aspect of this may be the widespread discussion of the necessity to integrate the NPOs in the planning process of governmental agencies. The concept of "planned development" is important for the social democratic way of thinking. In one perspective, such participation is enhancing the status of the NPOs as "partners" of the government and their possibilities to influence governmental decisions. To a certain extent, it is quite clear that such participation is absolutely necessary. The Norwegian Confederation of Sports, for example, has actively engaged itself in making such participation in the governmental planning processes possible for its officers at the local levels. Again, on the other hand, the question may be when NPOs will end up as some kind of quasi-governmental sector.

THE "MORAL" SECTOR AS LAWBREAKERS

Humanitarian organizations traditionally constitute a large part of the third sector. Therefore, the third sector institutions have often been regarded as more moral or idealistic than e.g. for-profit organizations. One of the results of the legislator not taking sufficient care of adjusting legal requirements to the distinctive features of the third sector, is that these institutions often violate the law. As in most other countries, even rather minor violations of the Norwegian tax legislation, for example, may often be liable to criminal proceedings. The common opinion, to a certain extent supported by research, is that NPOs very often break the rules, and that these violations are not prosecuted due to some kind of "gentlemen's agreement". There seems to be an informal common understanding shared by many government insepctors etc, that the rules are too strict and put unreasonably bureaucratic pressure on the organisations.[11]

Labor law is another area where NPOs probably very often violate the rules without any action being taken by the competent authorities, in spite of the strict sanctions imposed by the law. The Norwegian Labor Act 1977 may be taken as one of the legislative symbols of Norway as a social democratic country. The perspective is very much that of the employee. The purpose is to protect from the dangers of work. The positive aspects of leisure time are more or less taken as a matter of course. The need to engage employees also in their spare time to avoid idleness, is not passed upon by the legislator. Therefore, this is another piece of Norwegian legislation where there are no adjustments to the special needs of voluntary organizations. The paradoxes are very clear when it comes to the strict working hours regulations. For instance, there are general prohibitions against night work from 9 pm until 6 am the next day, and against work on holidays from 6 pm the day before the holiday until 10 pm on the holiday.[12] There are exempting rules for which in some instances also some NPOs may qualify. But, for lack of a general exemption for NPOs, they will often have to apply for special permits from the labor law authorities if they want to make use of ordinary staff at late evening hours or on holidays. There is no research supporting the hypothesis that NPOs break the rules and therefore risk criminal proceedings. But this is widely held to be the case. Labor law may be another aspect of legislation where the third sector is treated as some kind of *subordinate* sector. It has to submit to legislation primarily made for the market or for the governmental sectors. The result is that it has to behave as a law-breaker and becomes dependent on some kind of implicit goodwill from the authorities.

The implications of this tension between general, but higly detailed and strict legislation, and the distinctive features of the NPOs are many, but mostly of a very speculative nature. Attitudes of not taking the law too seriously may be generalized, there may be difficulties in recruiting leaders who will take the responsibilities of signing annual reports etc.[13] Most relevant to the main issue of this paper is the prospect of many NPOs being dependent on some kind of leniency by the tax authorities and other officials.

NPOS AS QUASI-GOVERNMENTAL COMPROMISES

In Norway, as in many other countries with largely expanding governmental sectors during the last decades, the question of reversing the process through reprivatization and privatization has become more vital. The present social democratic government has stated that it seeks "new models of cooperation between the government and, for example, non-profit, voluntary organisations".[14] This tendency is also witnessed in other countries reaching the limits of the welfare which the welfare *state* may possibly provide. Instead of allowing ordinary commercial enterprises to enter into e.g. the *health* industry, it is a more acceptable alternative for a social democratic ideology to open the activities to NPOs. In Norway, there has been a long tradition of NPOs running health institutions. The way of reasoning pointed out here is exposed in the difficulties that newly established private for-profit medical institutions have faced in gaining the political acceptance necessary to obtain any kind of public funding. In Norway, however, there has for a long time been a state monopoly in *broadcasting*, both for television and radio. In 1980 this monopoly was somewhat relaxed, opening for licences for private local broadcasting. In 1987, when the system with private local broadcasting was made permanent, ordinary for-profit organisations and other media businesses, e.g. newspapers, were not supposed to qualify for a licence directly.[15]

Privatization through NPOs may be seen as a way of strengthening the third sector. However, it may sometimes seem as if the "NPO-privatization model" is not so much chosen because of the attributes of the NPOs themselves. It may appear to be more a matter of the lesser evil; i.e. they are less different from the government and public sectors than for-profit enterprises. In some ways, especially in the case of broadcasting, the NPOs may end up as some kind of quasi-governmental agents. In one perspective, by allowing only non profits to run local broadcasting, one opens for privatization without really doing it; i.e. the state monopoly is allowed to continue without a really resourceful and dangerous national competitor. Recent political development may imply that this compromise will not hold and that the privatization will continue, also involving more traditional for-profit concepts. Still, the privatization of broadcasting in Norway may serve to illustrate how a social democratic state may use NPOs as some kind of compromise to hold off the challenges from for-profit enterprises against state monopolies and governmental privilиges.

THE WAR EXPERIENCE - NPOS AS ALTERNATIVE NETWORKS

In this paper, I have pointed to the not surprising conclusion that in a widely regulated and expanding social democratic state, the "independent sector" will have problems guarding its independence. "Indpendence" will also, from an economic and pragmatic point of view, matter less than the willingness to cooperate with governmental agencies and adjust to governmental plans. Another matter of concern in Norway is that large parts of the legislation affecting NPOs do not take the distinctiveness of the third sector into account. The social democratic way of thinking has often been thinking in dichotomies of state vs. market, employer vs. employees, taxpayers vs. government etc.

However, as pointed out earlier, the history of the third sector in most countries is highly complex and a result of long historical trends.[16] In Norway, the idea of the necessity of a strong independent nonprofit sector was emphasized during WW2. The civil resistance against the German occupants found some of its basis in the NPOs, which offered an alternative network when the public sector was controlled by the Germans.[17] This fact is one of the many reasons why the idea of a strong independent third sector may seem to take on a life of its own, somewhat independent of the political ideologies which may dominate during some periods.

Apart from such historical occasions which may prove the value of independent NPOs, beyond any doubt, the research needs in a social democratic country like Norway seem to be to point out the increasing dependency by NPOs on the state, and the consequences of this. Such research will have to go into unforeseen consequences of different kinds of legislation and subsidizing procedures. But, more basically, we need a clarification of the rationales for an independent - or at least "somewhat independent" - third sector in a state with vast governmental involvement in many spheres of life, - and much more statistical and empirical data on the role of NPOs.

NOTES:

1. Estelle James, "The Nonprofit Sector in Comparative Perspective", in The Nonprofit Sector. A Research Handbook, ed. by Walter J. Powell. New Haven: Yale University Press, 1987.

2. Parts of the information presented here will either be available in the Norwegian Statistical Yearbook published by the Central Bureau of Statistics in Norway or in the report to be published in 1988 by the Norwegian Commission on Nonprofit Organizations. In such instances, I do not offer citations. Also, in other instances I have kept citations to materials only available in Norwegian to a minimum.

3.The average subsidy ratio in Norwegian NPOs which might have given a basis for calculating the NPO-ratio of GDP has not been estimated. The subsidy ratio varies widely. NPOs running health institutions probably receive approx. 4 billion NOK, i.e. 65 per cent of the total subsidies to NPOs. These institutions usually receive subsidies covering 100 per cent of their operating expenses.

4. Income Tax Act art. 44 (5) which limits the deduction to maximum 10 per cent of net income or NOK 10.000.

5. Norsk Retstidende 1985 p. 929, Norsk Korrespondanseskole. For a more extensive discussion of the numbers quoted here, see Ole Gjems-Onstad, "Skattefrihet for undervisning og forskning", Skatterett 1986 pp. 61-92.

6. For a more detailed analysis, Oddvar Martinsen, "Overføringer mellom organisasjonene og det offentlige - utvikling og utprøving av analysemodeller for et nettooverføringsbegrep", Skatterett 1987: 152-174. For the introduction of the net transference concept, see Ole Gjems-Onstad, "Merverdiavgift og almennyttige institusjoner", Del 1 og 2, Skatterett 1987: 159-192, 278-323.

7. See the summary of the US discussion regarding income taxes, John G. Simon, "The Tax Treatment of Nonprofit Organizations: A Review of Federal and State Policies", in The Nonprofit Sector, A Research Handbook, ed. by Walter W. Powell, New Haven: Yale University Press, 1987. For a broad international presentation by advocates of the exemption point of view - the tax expenditure concept, see Paul R. McDaniel and Stanley S. Surrey, International Aspects of Tax Expenditures: A Comparative Study, Deventer, The

Netherlands: Kluwer, 1985, especially pp. 91-93. An introductory discussion of the tax expenditure concept relating to the Nordic countries is: Nordisk skatteutgiftsgruppen, Skatteutgifter, Nordisk ministerråd, 1987.

8. See Ole Gjems-Onstad, "Merverdiavgift og almennyttige institusjoner - Del 1 ", Skatterett 1986: 159-192, 163-66.

9. In administrative practice an object bought at NOK 20 was sold by the NPO at NOK 500. The transaction was not defined as a sale. In another decision, the object used as some kind of receipt had a value of NOK 0.30 and the "price" was NOK 20. See Gjems-Onstad 1986 supra p. 187.

10. See for example, Adult Education Act 1976 art. 10.

11. In a report by a working party in the Treasury, considering necessary simplifications regarding withholding tax and payroll tax, it was repeatedly stated that NPOs did not adhere to the rules - without any sanctions being imposed: "Forenklinger i reglene om skattetrekk, arbeidsgiveravgift og lønnsoppgaver", Innstilling av juli 1986 fra en arbeidsgruppe nedsatt av Finansdepartementet, 53, 55-56, 58-59. In a thesis made by two MBA students at the Norwegian School of Management, it was found that none of the five sports clubs inquired into, complied with the legal requirements regarding payroll and withholding tax. Two of the five clubs operated a completely "black" system. Most striking was perhaps how the officers of the clubs talked quite openly about this "natural" and "efficient" way of handling economic matters. The amounts involved were in no way insignificant. Ole Jørgen Baklid og Morten Solberg Nilsen, "Regnskap og kontroll i norske idrettslag", Diplomoppgave ved Bedriftsøkonomisk Institutt, (1987).

12. Labor Act 1977 art. 42 and 44.

13. As a student research assistant this writer was once offered the following piece of advice by an established professor of tax law: "Whatever you do in life, don't sign any annual report by a voluntary organisation!"

14. St. meld. nr. 4 1987-88 p. 87.

15. See draft of regulations dated December 12, 1987, supplementing Local Broadcasting Act 1987; and the parliament committee report, Innst. O. no. 3 1987-88; and the report by the Department of Culture, Ot. prp. no. 47 1986-87. Even though an ordinary business - for example a newspaper - may not be granted a licence, it may hold up to 49 per cent of the interest in a

qualifying organisation.

16. See for example, Helmut G. Anheier, "Indigenous Voluntary Associations, Nonprofits, and Development in Africa", in *The Nonprofit Sector, A Research Handbook*, ed. by Walter W. Powell, New Haven: Yale University Press, 1987.

17. See as the main work about this hypothesis the dissertation, Thomas Chr. Wyller: *Nyordning og motstand - Organisasjonenes politiske rolle under okkupasjonen*, Oslo: Universitetsforlaget, 1958.

WORKING DRAFT

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THE PUBLIC USE OF NONPROFIT ORGANIZATIONS ABROAD: SUBSIDIES, REGULATIONS AND PRIVATE SECTOR SIZE

by

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Many countries today are considering greater reliance on the private nonprofit sector for the provision of quasi-public goods, i.e. goods that yield both private and social benefits, such as education, health, and social services. It is argued that this would enable such services to grow without imposing additional costs on the public treasury. Furthermore, the discipline of the market would force private providers to operate efficiently and in accordance with consumer preferences. Thus, both developing countries and advanced industrial states are considering adopting policies designed to foster the growth of the private sector for providing quasi-public goods.

Before adopting new policies, it is useful to take stock of the old ones, a task which I attempt in this paper. I focus on the case of education; further research is needed to establish whether these results apply to other services provided by the nonprofit sector as well. In this paper, based on written documents and discussions with knowledgeable people about a sample of 35 advanced industrial and developing countries, as well as research visits to some of them, I outline the major policy constellations that currently exist.

While there are many dimensions to a country's policy toward private (and mostly nonprofit) education, two may be most salient: the degree and type of subsidy or financial support and the degree and type of regulation or control. Both of these create a kind of public-private hybrid, subsidies implying mixed public-private funding and regulations implying mixed public-private decision-making. In fact, pure private finance and management of education are rarely found. The private sector is defined in this paper as comprising all educational institutions which were privately founded and where some significant proportion of the financing and decision-making remains in private hands, even though government may provide partial resources and control.

What kind of subsidies do we find, what is the nature of the regulations and is there a connection between the two? Are there systematic relationships between the subsidy-regulation patterns and private sector size? These are the major questions addressed in this paper. Interestingly, the answers turn out to be diferent in modern and developing countries, a difference which stems from the contrasting nature of the demand for private services in these two cases. In my broader paper on this topic I also investigate which policies are consistent with alternative educational goals.(James 1987d)

I. Policies Toward Private Education in Developing and Advanced Industrial States

Data Problems

Data on types of subsidies, regulations and private sector size were obtained for a sample of 35 modern and developing countries, from combination of published sources (Mason, 1983; Neave, 1985; World Bank, 1986), visits to countries and discussions with knowledgeable officials. Data on this topic are difficult to secure; therefore a few problems should be mentioned at the outset.

First, in some countries there may be missing information on types of subsidies and regulations; that is, either or both may be understated in some cases. This could not be avoided without extensive research visits to each country. Partly for this reason, I have treated countries as groups, rather than as separate units; it is less likely that the missing information was large enough to distort the group assignment.

The second problem works in the opposite direction. My groups are based on subsidies and regulations "on the books." However, these are implemented in very different ways in different countries and I have much less information on degree of enforcement. To exemplify how important this factor is: we know that the enormous expansion of Japanese private education in the 1950's and 1960's was facilitated by a bureaucratic decision to overlook the many detailed regulations which specified space per student, minimum number of chairs and books, maximum student-faculty ratios, enrollment ceilings etc. Most of the numerous private universities that were established during this period simply did not meet the required standards, yet they were given official approval. This might appear to be a highly regulated system, but de factor it was unregulated, in these respects (Pempel, 1973; James and Benjamin, 1988).

The enforcement problem is especially great in developing countries. In Zambia, Nigeria, India and Pakistan numerous unregistered private schools have developed in recent years. Such schools may not meet all of the registration requirements but they apparently meet consumer requirements nevertheless (see Kaluba, 1986). As yet another example: similar detailed regulations are in effect in Colombia but systematic monitoring is impossible, especially since the number of private institutions has increased much faster than the administrative-inspection staff. Thus, the regulations are enforced sporadically and may appear as a nuisance factor rather than as constructive oversight. The very presence of numerous regulations "on the books" does indeed open the door to harassment, corruption and other restrictions on private initiative, even if they are not systematically enforced. This would be worth further investigation in several countries. For the purposes of this paper, however, I assume a uniform level of implementation, unless I have specific information to the contrary.

As a third problem: there are often two separate private subsectors, one heavily funded and controlled, the other unsubsidized and relatively unregulated. Sometimes the unaided schools are there by choice because they do not want to accept the control that goes with aid. More often they are there because the government does not want to aid them. In the discussion below I sometimes distinguish between the two components of the private sector but generally I have categorized each country according to its average treatment of the sector as a whole, which depends on the relative size of the two component parts.

Finally, countries frequently have different policies toward the private sectors at primary, secondary and higher levels, and the size of their private sectors also vary by level. For purposes of expositional simplicity, I concentrate this discussion on the secondary level, except where otherwise noted.

Subsidies and Regulations: A Diagrammatic Representation

In this section I summarize my data on subsidies, controls and private sector size. Ideally, I would like to have ranked each country according to its ratio of subsidy to total private sector cost. However, data on size of subsidy and/or total expenditure were not available for most countries; private schools jealously guard their financial information. Therefore, a rougher grouping was used. Countries were placed into four categories of roughly equal size: I. Those which offer no systematic subsidy; II. Those which offer indirect subsidy; III. Those which offer partial subsidy; and IV. Those which offer almost complete subsidy (over 75% of total costs) to their private educational sector.

Table 1 lists the kinds of subsidies found in each category. While category I obviously offers the least aggregate subsidies and category IV the most, the value of the implicit subsidy in category II sometimes exceeds the explicit subsidy in category III. (Both of these categories offer subsidies that are less than 25% of total costs, though difficult to quantify precisely).

Ranking countries according to degree of regulation was more difficult, because of the complex, varied and detailed nature of controls, which cannot easily be collapsed into a single scalar value. I found, however, that certain types of control were almost universal (Regulations of Physical Facilities), others exist in a large set of countries (Academic Regulations, Organizational and Reporting Requirements), and still others apply mainly to countries and schools where large subsidies are granted (Regulations Regarding Teachers and Students). I was thus able to construct a (rough) continuum with respect to regulation as well.

Table 2 lists the regulations I found, in this order; they represent the decision-space that has been shifted from the private to the public domain. Some elements of category I (Regulations of Physical Facilities) generally appear before II A (Academic Regulations) or II B (Organizational and Reporting Requirements), and II always appears before III (Regulations Regarding Teachers and Students), so that III implies some elements of I and II are present, but it is possible that II B will appear without II A, as noted below. A fourth category lists the kinds of decisions that are almost always reserved to the schools.

We can now construct a scatter diagram, which depicts each country's policies in 2-dimensional space and tells us what, if any, are the relationships between subsidy, regulation and private sector size. In Figure I degree of subsidy is measured along the horizontal axis and degree of control along the vertical axis. Thus, the upper right hand (Northeast) corner represents a pure public system: full public funding and control. The lower left hand (Southwest) corner represents a pure private system: full private funding and control. As we have just suggested, however, most private schools are hybrids, receiving some public support and/or facing some public regulation, and therefore fall somewhere between these two extremes.

In this diagram, a square indicates a developing country and a circle indicates a developed country. When these are filled in they represent large private sectors (20% or more of total enrollments) and when blank they represent small private sectors at the secondary school level. (Of course these numbers would be somewhat different at the primary school or university levels). The diagram is used for illustrative purposes only. Thus, the circles and squares total more than 35 because some countries were counted more than once, before and after major policy changes occurred in the 1970's or by two different states within a given country or by two different subsectors with very different degrees of subsidy and control.

The diagram depicts the following groups of countries:

I. No systematic support. (Row 1, along the horizontal axis.) This group, which includes several African and European countries (e.g. Nigeria, Madagascar, Mali, Burundi, Algeria, Sweden, Greece, Italy), gives virtually no assistance to private schools on a regular basis. Nevertheless, those which exist often face both physical and academic regulations. They are required to register, to meet minimum health and safety standards and, if a national curriculum, exam system or timetable exists they are required to follow it despite the absence of subsidies (e.g. Italy, Greece). These regulations are costly, both in terms of money and organizational time and effort. Consequently, the net attitude toward private schools might be termed negative, sometimes the result of an antagonist political ideology. Indeed, these controls are often designed to discourage or prohibit private schooling, as in Pakistan and Tanzania in the 1970's. Thus, the private sector in this group is usually small (i.e. blank circles and squares).

II. Indirect subsidy. (Row 2.) This group, which includes the U.S., the U.K., Jordan, S. Korea, the Philippines, Japan before 1970 and several Latin American countries (Brazil, Mexico, Guatemala), offers indirect subsidies to the private sector: tax privileges (e.g. relief from import duties, property tax, income tax, gift tax, sales or value-added tax); low interest, tax-free or government-guaranteed loans; and student loans or special scholarships (especially at the university level) which enable students to pay high fees. Of course, tax benefits have value only if the country has a well functioning tax collection system and student loans will work only if they are ultimately repaid. Both these requirements limit the usefulness of indirect subsidies in developing countries. On the other hand, government guaranteed or subsidized loans may be a useful way of overcoming capital market failure problems, especially acute at the higher educational level. Several of these countries also indirectly facilitate private sector growth at the university level by charging substantial fees at public universities (U.S., Korea, Japan).

Interestingly, some of the "indirect subsidy" countries do not impose national degree requirements, examinations or even a national curriculum on their public or private schools; weak central control of education is characteristic of such countries which may also help explain their reliance on indirect forms of subsidy (e.g. the U.S. and U.K. are prime examples). On the other hand, regulations of physical facilities as well as organizational, procedural and reporting requirements are typical of this group. This may be viewed as an attempt to provide information and incentives that lead schools (the agents) to act in the interest of the government or society (the principal) without extensive direct controls.

For example, in the U.S. all schools are subject to zoning and building codes and annual financial statements are required for those which wish to retain tax exempt status. This is a significant requirement, since private schools are reluctant to provide information on their revenues and costs in most countries, fearing that it will be used against them (see Kagan, 1986, for other structural and procedural requirements in the U.S.). In Japan, S. Korea and parts of Latin America nonprofit status is required for all private schools and universities and in the U.S. and U.K. it is, again, a necessary condition for tax-exemption. As discussed in my broader paper, this requirement may be motivated by the belief that it will help to safeguard quality.

In Brazil, Colombia and Guatemala starting fees and any subsequent changes must be approved by the government and detailed financial reports are required for this purpose. Such regulation of fees is unusual in unsubsidized schools and could be a significant impediment to private sector growth, if enforced. Nevertheless, it is widely believed that schools usually find their way around these restrictions, e.g. by invoking "voluntary" contributions, charges for transport and meals, etc. The reporting regulations, however, remain.

In developing countries excess demand is usually large enough at the secondary and higher levels to produce large private sectors in this relatively permissive atmosphere and these are shown by the filled in squares in row 2 of the diagram. In developed states, however, the private sector is relatively small in the absence of direct subsidies and therefore is shown by blank circles.

III. The partial subsidy group. (Row 3.) A wide variety of countries offer partial subsidies (less than 25% of total expenses to their private educational sector. Examples are Senegal, Peru and Bolivia (especially to the "fe y allegria" schools and cooperatives), Pakistan (after 1980), Japan (after 1970), Jordan (primary level), Liberia, Indonesia, Kenya, and some Indian states. (Education is reserved to the states, not the central government in India, and state policies differ widely.) Most commonly, the subsidy includes in kind provision of books, supplies and meals; 1 or 2 teachers per school; and subsidized teacher-training. Often a cash grant is given as well; less often, low-rent buildings or shared facilities (e.g. libraries) and indirect subsidies such as tax incentives are included. In Kenya, Paraguay, and several other countries rural communities have started their own schools, then pressure the government to provide teachers, with partial success.

The regulations which accompany these subsidies range from minimal to broad controls over physical facilities, fees and salaries of subsidized teachers (e.g. these apply to subsidized schools in Peru and Senegal). These countries apparently do not believe that indirect structural and reporting requirements will suffice to bring private school behavior into concordance with government interests, either because private consumers and managers have different information about the production function of educational quality because they have different goals. On ther other hand, these countries do not regulate too heavily, for fear that private initiative will be discouraged.

For example, in Indonesia schools must spend more than their private sources of income in order to be eligible for aid; i.e. aid cannot exceed their operating deficit. In this sense, subsidized schools are turned into nonprofit (or zero-profit) organizations. Beyond that, subsidized schools must have at least two permanent qualified teachers (as evidence of quality), and Indonesian must be its language of instruction (a tool of national unity). Similarly, Pakistan has stated its intention of making Urdu (or an approved provincial language) the instructional medium in all schools. This is important because desire for English medium instruction is a major source of private sector demand in many countries (e.g. Pakistan, India, Latin America) and such regulations, therefore, undercut the potential market. It should be noted, however, that even in countries with these nationalistic requirements, some of the most elite private schools are exempted, teach a foreign curriculum in English and prepare students for external examinations (e.g. in Pakistan a few such schools are heavily subsidized).

Sometimes indirect regulation exists in these countries via the type of schools for which partial aid is designated. For example, the fe y allegria schools which are subsidized in many Latin American countries are run by Catholic orders specifically for low income groups in urban areas; with admissions policies and fees self-regulated for this purpose, external regulation is unnecessary and superfluous.

Almost all of the countries in this in-between category are developing. In general, the positive effects of the partial subsidies outweigh the negative effects of the moderate controls, so most of these countries have large excess-demand driven private sectors, as depicted by the filled in squares in the third row of the diagram.

IV. The high subsidy group. (Row 4.) Here we have a concentration of developed countries (Holland, Belgium, France, Luxemburg, Denmark, Norway, New Zealand, the "voluntary aided" schools in the U.K., the "substitute" schools in Germany) which provide heavy subsidies, covering over 75% of total expenses, to their private schools, usually differentiated along religious lines. Included here too are the state of Kerala in India, Lesotho, Togo and Chile. In particular, all teacher salaries are paid in these countries, an allocation (usually based on enrollments) is made for other recurrent expenses, and a high but varying proportion of capital costs is also covered. In the case of Chile, payments are made per student, in a modified voucher plan, but the net effect is the same. Generally, the intent is for private and public schools to operate at the same level of expenditure per student in these countries.

It is hardly surprising that these are also the most heavily regulated schools. Besides the physical, academic and financial controls that we have already encountered, these schools often face controls over teacher salaries, credentials and procedures for hiring and firing as well; private school teachers, in effect, have the same status and job security as civil servants (e.g. Holland, France, and to a lesser extent Belgium). Government sets and pays teacher salaries in Togo and Lesotho. Also of interest are regulations designed to control the decision-making structure, by placing teachers, parents, students and government representatives on the governing boards (e.g. Holland, France, voluntary aided schools in U.K.). This is designed to ensure democratic accountability in a situation where public funds and production responsibilities are turned over to private organizations.

Controls extend too over the distribution of service and the criteria for selecting students in heavily subsidized schools, in an attempt to deal with problems of equity and access and to limit "creaming" of the best students by the private school. For example, academic ability could not be used as grounds for exclusion in English voluntary aided schools, after the public shift to comprehensives. In France private schools are eligible for subsidy only if they agree to become part of the regional educational plan; the government's attempt to require them to accept students assigned from their catchment area sparked a major and as yet unresolved controversy. The price for government support to the mission schools in post-independence Kenya and for state support of denominational schools in post-war Germany was that they agreed to forego religion as a basis for selection; schools that receive aid must use centrally-determined selection criteria. [Interestingly other countries specifically permit religious selection of students and teachers in their subsidized private schools and some countries (e.g. Kenya, Nigeria, Malaysia, India) use tribal, caste or regional quotas in their public schools as well.]

In general, price-rationing is restricted or proscribed in high-subsidy schools. This is especially significant because a ceiling on fees implicitly places a ceiling on expenditures per student and therefore on school quality. Holland places a low ceiling on fees and students cannot be excluded on grounds of nonpayment. Governmental approval of fees is required in Luxemburg. Subsidized schools in Chile and voluntary aided schools in England cannot charge fees. In India tuition floors are set in some states, ceilings in others, for aided schools, reflecting different philosophies about whether the regulations are designed to enhance resources and quality (floors) or equality (ceilings).

This leads us to the point that in almost all cases, even as a public funding approaches 100%, the final selection of teachers and students as well as teaching method is left to the school; this seems to be the sine qua non of "private" education. But this is also most important, because the students plus the teachers and the teaching method ultimately determine the learning environment. When these decisions, too, are turned over to the government, the private schools have been nationalized.[1]

As indicated by the above examples, many of the countries in the higher subsidy group are developed, although a few developing countries are also represented. This category contains a mixture of large and small private sectors, depicted by the filled in and blank circles and a few squares in the top row of the diagram.

Part II. Relationship Between Subsidies and Private Sector Size: Modern Versus Developing Countries

A casual perusal of Figure I shows that the countries in my sample fall into two clusters rather than a continuum of countries: those offering low subsidies (less than 25% of total sector expenditure) and those offering high subsidies (more than 75% of total sector expenditure).[2] But whether we look at the low or the high subsidy clusters, we observe that about half of the countries have large private educational sectors and half small. In this simple sense, there is no clear-cut relationship between rate of subsidy and private sector size.

However, if we disaggregate between developing countries (squares) and advanced industrial countries (circles), the picture changes. First of all, the modern countries are divided equally between the high and low subsidy clusters, while most developing countries fall into the latter category. Historically, many 19th century European countries would have fallen into the latter group as well. This suggests that private sectors in developing countries are more "pure" than those in modern countries, and depend mainly on fee financing, while subsidies, regulations, and hybridization increase in the process of economic development.

Second, many private educational sectors in developing countries are "large", e.g., more than 20% of secondary enrollments are in private schools, while most private sectors in modern countries are relatively small. Third, some developing countries in the low subsidy cluster have large private educational sectors; while all modern countries with large private sectors are located in the high subsidy cluster--although high subsidy does not guarantee large private enrollments. Thus, when we look separately at developing countries and advanced industrial states, we find a more positive relationship between subsidy and private sector size, particularly for the latter. Subsidies are a necessary but not a sufficient condition for large private school sectors in advanced industrial states.

This shows up most clearly when we examine the low subsidy cluster, which contains a few modern countries and some "suppressive" developing countries (i.e. no systematic assistance, many regulations) both of which, consequently, have small private sectors. More surprisingly, we also find a large number of "permissive" (low subsidy, low regulation) developing countries with large private sectors. That is, large

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private sectors occur with low subsidies as well as high subsidies, but the former are all from developing countries.

How can large private sectors grow without substantial public support? This runs counter to the belief of many educators and economists, who emphasize the need for public spending to increase enrollments. This puzzle is solved once we examine the source of demand for private education. As I have shown elsewhere, in developing countries the private sector is a response to excess demand (James, 1987a and 1987c). Because of limited resources, the public sector does not provide a place for everyone, particularly at the secondary and higher levels. However, the private rate of return is high because education brings better jobs and lifetime earnings. As a result, many people are willing to pay the price necessary to acquire an education in the private sector. This is why we find large private educational sectors in many development countries.

Excess demand and private sector size will be particularly large if the government has adopted a high-quality low-quantity pattern for the public sector. In a regression analysis I conducted across 38 developing countries, a small supply of public school places led to a large private sector, consistent with my theory of excess demand (James 1987c). In choosing the capacity of the public sector then, the government is also making a policy choice about the size of the private sector. The scarcity of resources in developing countries keeps subsidies to the private sector low. Nevertheless, when public supply is limited and excess demand expands, subsidies are not necessary for growth; private education will flourish in an atmosphere of "benign neglect."

By contrast, in most advanced industrial societies (Japan being a major exception), a public school place is provided for everyone, at least at the primary and secondary levels; hence there is no excess demand. Instead, as I have shown elsewhere, heterogeneous demand is the motive for private education, i.e., some people want an education which is differentiated along religious, linguistic, pedagogical or academic quality lines from that provided by the government. But, since fee-charging private schools must compete against freely-available public schools, their effective demand is immediately limited. Therefore, the private sector will not grow large in advanced industrial societies unless it is heavily subsidized, so that the state rather than the individual pays most of the bill.

And, wealthy countries can more easily afford generous subsidies. As resources for education increase, some of them are used to subsidize private education. Elsewhere I have argued that this subsidization is a response to political pressure from consumers who want a differentiated product and from producers, often powerful religious organizations, who want to maintain a clientele for their schools (James, 1987b and 1987c). Therefore, many modern countries are in the high-subsidy cluster (Northeast quadrant) and we observe that several of these have large private sectors.

But not all private sectors in the high subsidy cluster are large.

In culturally homogeneous countries such as Norway or Luxemburg there is little differentiated demand for education so the private sector will be small even if subsidies are available, because a uniform public product can be offered which is consistent with consumer tastes. Just as the absence of subsidies does not rule out large private sectors when the underlying (excess) demand exists, so it does not create large sectors when the underlying (differentiated) demand does not exist.[3]

Along similar lines, in a regression analysis I conducted across 12 modern countries the existence of large subsidies was positively related to private sector size, but religious and linguistic heterogeneity were additional important explanatory factors, as expected. (James, 1987c)

Part III. Relationship Between Subsidies and Controls

As we have seen, the state is in a position to control even without subsidizing. In particular, minimum health and safety standards may be specified (consistent with general building codes and additionally to protect children) and a national curriculum, degree requirements and examinations may be imposed (to preserve national unity and integration). Schools that do not comply can simply be closed down or can be deemed as not acceptable for meeting compulsory attendance laws. Voluntary or mandatory licensure or accreditation procedures can also exist without aid. Such situations of the stick without the carrot are indicated by the points along the horizontal axis; in most instances, if the regulations are enforced, the resulting private sectors are small.

At the level of moderate subsidies we see considerable reporting requirements but no clear-cut increase in direct control. Such situations (rows 2 and 3) mainly signal a more hospitable government attitude toward the private sector. It is also possible that the existing controls are more strictly enforced over recipients of subsidies. For example, within the U.S. controls over teacher certification and curriculum requirements are enforced more strongly in those states which aid private schools and enforcement has increased over time as aid has increased (Encarnation, 1983). Unfortunately, as noted above, it is difficult to get this kind of information on enforcement for a large set of countries.

Finally, once large subsidies are granted, substantial additional regulations follow in virtually all cases. In this sense there is a positive relationship between subsidies and control; as we move north toward very high subsidies we also move east toward greater regulation in Figure I. As we saw above, these controls ultimately cover teachers' salaries and credentials, criteria for selecting students, fees, and decision-making structure.

The normative rationale for these regulations is that, once public funds garnered by compulsory taxation are given, society also has the right (duty) to exert some control over how these funds are spent. Private schools should not be able to do things with public funds that would be ruled out of bounds to the public schools, which are presumably being run to maximize social welfare. This is particularly the case if subsidies combined with autonomy give private schools a competitive advantage over public schools; the regulations limit that advantage.

The desire for control may also be part of the raison d'etre for the subsidy. If we regard central government as the principal whose goal it is to maximize social welfare, and private school managers as the agents, differing objectives and information may lead agent behavior to conflict with that preferred by the principal, in which case direct controls may be in the public interest. The large subsidies enable the controls (which are costly) to be imposed without fear of driving away most private entrepreneurs. In this sense, the subsidies may be a necessary cost if a society wants the variety and competition associated with privately produced education but also wants tight social control over variables such as quality and distribution.[4]

A positive rationale for the regulations is that, once having given funds, politicians have the power to demand a quid pro quo, and they use this power to establish rules and standards that gain them good will from diverse constituencies and hence help them get reelected (whether or not this maximizes social welfare). In this connection, it is significant that many government regulations, particularly those that are closely tied to subsidies, apply to inputs or to the distribution of service rather than to the outputs themselves. Thus the academic regulations may exist with or without subsidy, but price controls and tight regulations of teachers usually exist only if subsidies are present. For example, the numbers, salaries and credentials of teachers in subsidized schools are usually regulated, as are hours and other conditions of work. We also find rigid restrictions on the school's ability to fire teachers.[5]

The emphasis on inputs may stem partially from the fact that inputs are easier to control and measure than outputs; these regulations may be used in situations where inputs are readily observable but outputs (including quality) are not. But more basically, this phenomenon is consistent with the view that regulations will generally serve a mixture of interest groups (see Peltzman, 1976 and Stigler,1971). Whereas economic efficiency arguments are usually counched in terms of consumer interests, these data suggest that producer and worker interests are equally important in the political process which creates and maintains the subsidies and the accompanying regulations. For example, in Kerala, India, subsidies to private (religious) schools were introduced in the 1960's by a socialist government, despite its ideological opposition to religion and privatization, because it wanted to pay a political debt to its supporters in the teachers union. A requirement to raise teachers' salaries substantially, accompanied the subsidies. While the higher salaries may have enabled better teachers to be hired at the margin, much of the increase went to the existing teaching staff and therefore constituted an income redistribution to them. (Conversely, allowing the growth of unsubsidized private schools is one politically feasible way that societies sometimes use to economize on teacher costs).

As a result, costs rise dramatically when subsidies are instituted and wages rise fastest of all. This has been demonstrated in my studies of Japan, Holland, Sweden and Australia, the few countries where I was able to get the necessary data (see James, 1982, 1984, 1987b; James and Benjamin, 1988). Thus, cost advantage may be one raison d'etre for reliance on private education in developing countries and for reliance on nonprofit production of other quasi-public services in the modern welfare state, but ironically, this cost advantage is likely to disappear if large subsidies are introduced--in part because of the regulations that accompany (or follow) the subsidies.

IV. Conclusion

In summary, I have found that private educational sectors in developing countries tend to be less subsidized (and less controlled) than in developed countries, yet they are also larger. This apparent paradox is resolved when we look at the source of demand for private education: Private sectors can flourish in developing countries without subsidies, because of excess demand from potential consumers, while subsidies are a necessary condition for large private sectors in developed countries, where a free public alternative usually exists. This disaggregaton is necessary in order to uncover the true relationship between subsidy and private sector size.

I have also found that regulations, particularly over inputs, distribution of service and price, usually accompany large scale subsidies to private education. The same political and economic forces that lead politicians to impose regulations over government services lead them to regulate government-funded services, even if these are privately produced. In the U.S., schools and universities bemoan the costs and constraints implied by these regulations. However, we have seen that some of the most significant output decisions are left to the private schools, which are still allowed to compete with each other on this basis, thereby preserving variety and choice, even if complete autonomy has been surrendered. Presumably the schools feel the funds are worth more than their loss of autonomy and government feels that the controls are a sufficient price for the funds, both parties being both off as a result of the trade.

Thus, in developing countries privatization policies can increase both private finance and management of education, but in modern countries privatization policies may shift production to the private sector only if accompanied by substantial public funds and controls. While the empirical data in this paper has come from the education industry, a similar disaggregation between excess demand and differentiated demand situations, between industries where fee financing is and is not viable, may be needed to understand the possibility of increasing the role of the private nonprofit sector providing other quasi-public services as well.

Footnotes

The author is Professor of Economics, S.U.N.Y., Stony Brook and Guest Scholar, Brookings Institution. This paper was adapted from part of a report prepared for the World Bank as part of its program for analyzing decentralization. The first draft was written while I was a fellow at the Netherlands Institute for Advanced Study. I wish to thank the many people at the World Bank and elsewhere with whom I discussed this topic and the many people in developing countries who answered the questionnaire or sent me related information. These include: George Psacharopoulos, Emmanuel Jimenez, Jee Peng Tan, Bernardo Kugler, Nestor Dominquez, Ernesto Schiefelbein, Jack Maas, Robert Drysdale, Michael Mertaugh, Donald Winkler, Linda Dove, Adriaan Verspoor, Celicia Valdivieso, Tufan Kolan, Himelda Martinez, Manuel Zymelman, Adriano Arcelo, Andrew Urevbu, Vandhyala B.G. Tilak, C. de Moura Castro, Shahrukh R. Khan, Hashim Abrasi, Kiong Hock Lee, Eduardo Velez, Sylvia Schmelkes and George Eshiwani. Guy Neave at the Institute of Education, University of London, was also very helpful providing me with information on European countries. Vinh Nguyen drafted the grafts.

1. As, indeed, happened to many private (girls') schools in Sweden in the 1920's, in Bijar state (India) and in Pakistan in the 1970's, to mission schools in several African countries when they became independent, and to primary schools in S. Korea in 1980.

2. Australia, whose subsidies are greater than 25% but less than 75%, is an exception which lies somewhere in the middle, with a large private sector. However, subsidies are a relatively new phenomenon in Australia so an equilibrium has not yet been reached. I predict that its subsidies (and regulations) will gradually move to the upper range.

3. Also, entry to subsidized status is severely limited in most of these countries, keeping the private sector smaller than it would have been with free entry. For example, in some countries only schools which are run by a religious denomination and which meet rigid government guidelines can qualify.

4. In some cases, private schools have rejected the regulations and given up the subsidies that go with them. For example, most "direct-grant" schools (except for the Catholic ones) chose to become fully independent rather than accepting "voluntary aided" status when this choice was given to them in England, in the late 1970's. Similarly, in Australia some private schools which now receive small subsidies are making contingency plans to forego them if the regulations become too onerous. In Kenya, at least one religious community requested that its schools be released from "aided" status--and set up a separate, unaided, uncontrolled school when this permission was denied. In New Zealand, schools were recently offered a menu of choices featuring different degrees of subsidy plus control and some chose the low option. However, most schools have accepted the regulations together with the subsidies, thus generating the large hybrid private sectors that we find in most advanced industrial societies today.

5. This emphasis on regulations over inputs rather than outputs may explain why Kramer (1981) did not find that a high degree of control accompanies subsidies in the social services. He was looking [illegible] at outputs while I am looking at a broader range of regulations.

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Table I

Subsidy Constellations and Their Ingredients

I No Systematic Subsidy

II Indirect Subsidy
- Tax benefits (relief from import duties, property tax, sales tax, income tax, gift tax)
- Low-interest loans or guaranteed loans
- Student loans or scholarships

III Partial Subsidy
- In-kind provision of texts, meals, supplies, some equipment
- Provision of 1 or 2 teachers per school
- Subsidized teacher-training
- Small cash grant
- Low-rent buildings or shared facilites

IV Almost Complete Subsidy
- Payment of all teacher salaries
- Other recurrent expenses, depending on enrollment
- High proportion of capital costs

Table II

Types of Regulations, According to Probable Occurrence

I Regulations of Physical Facilities

- Schools must register
- Health and safety standards must be met
- Standards regarding space and furniture must be met
- Target enrollments are related to physical facilities

II A. Academic Regulations

- Schools must follow detailed government curriculum
- Degree requirements are specified by government
- Calendar and timetable are specified by government
- Students must take national exams periodically (e.g. at exit from primary and secondary school or entrance to public secondary schools and universities)
- Medium of instruction is specified *

II B. Organizational and Reporting Requirements

- Schools must have non-profit status
- Schools must submit periodic financial reports
- Minimum investment is specified *

III Teachers and Students

- Teacher salaries and qualifications are specified by government
- Procedures and criterion for firing teachers are specified by government
- Allocation of budget between teachers and other inputs is specified
- Fees are controlled by the government
- Expenditures per student are limited
- Critera and procedures for selecting students are specified
- Government representatives serve on managing board of school

IV Decisions Generally Reserved to Schools

- Selection of teachers
- Selection of students**
- Teaching methods
- Religious instruction

* These regulations are rare, but potentially important.

** Some societies do not permit religion or ethnicity as grounds for selection: others explicitly permit it. This regulation does not occur in any regular order.

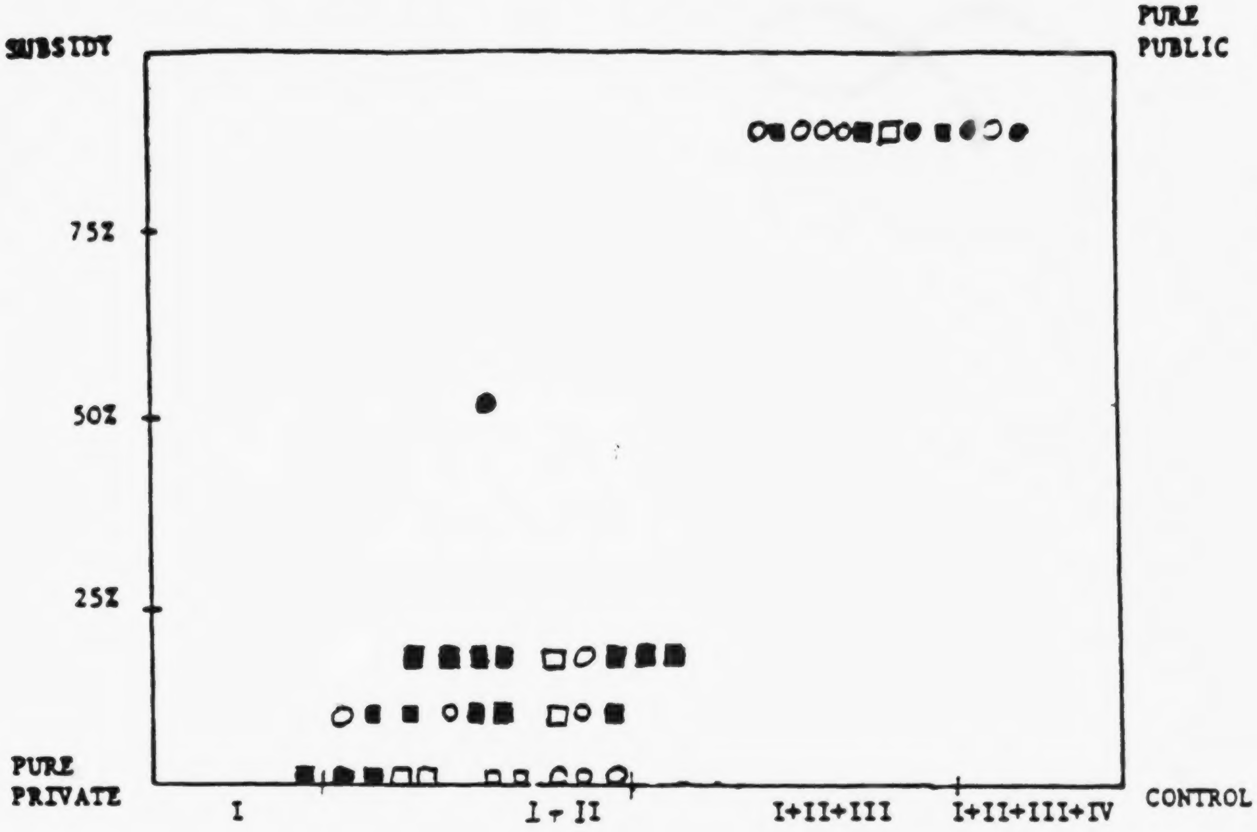

FIGURE I: POLICY CONSTELLATIONS
SUBSIDIES, CONTROLS AND PRIVATE SECTOR
SIZE IN MODERN AND DEVELOPING COUNTRIES

○ = Advanced industrial state with small private sector.
● = Advanced industrial state with large private sector.
□ = Developing country with small private sector.
■ = Developing country with large private sector.

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SECTION TWELVE

ISSUES IN CORPORATE GIVING

Cause-Related Marketing: Here to Stay or a Passing Fad?

by Kathleen A. Krentler 610

Workplace Fundraising: How Changes in the Donor Base, the Workplace and Non-Profits Will Affect Workplace Charities and Their Sponsoring Employers

by Steven L. Paprocki 622

Corporate Contributions to the Year 2000: Is a Slowing of Growth Inevitable?

by Hayden W. Smith 632

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CAUSE-RELATED MARKETING: HERE TO STAY OR A PASSING FAD?

by

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Prepared for the 1988 Spring Research Forum
"Looking Forward to the Year 2000:
Public Policy and Philanthropy"

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Introduction

The term cause-related marketing is a hot buzzword currently being bandied about the public and nonprofit sector as well as the corporate world. The attention the phenomenon is receiving appears to be only about five years old. The term itself appears to have originated within the American Express Corporation, coined to describe a number of activities that firm had undertaken that were designed to benefit both themselves and an assortment of social and philanthropic causes. The concept of cause-related marketing has grown beyond the scope of this single corporation, however, and is today being hailed or criticized (depending upon the source) as a new form of marketing that brings the activities of the public and private sectors closer together.

This paper examines the phenomenon that is coming to be known as cause-related marketing. Its proponents and opponents appear equally vociferous in defending it as the long awaited messiah for both the public and private sectors, or conversely, criticizing it as the devil incarnate of commercialism, tainting both sectors equally. The truth, most probably, lies in the region between these two extreme positions. Consideration of several pertinent issues will help address the benefits as well as the hazards of this new concept and thus provide for an informed assessment of whether it is indeed a passing fad or not.

Distinguishing Cause-Related Marketing

Cause-related marketing is not simply a new name given to the social and philanthropic activities of private sector corporations. The latter emanate from companies who have long felt that they had a moral obligation to put something back into the community (both locally and on larger scales) from which their profits came. This activity in most instances is at least partially inspired by the firm's desire to be socially responsible. Beyond this moral and social responsibility it cannot be overlooked that such activities are typically seen as benefitting corporate image and resulting in some long run, general benefit to the firm. This benefit may or may not be directly related to increased revenues for the firm. Corporate image, however, is generally enhanced through philanthropic activities that typically take the form of direct donations to the nonprofit organization.

Cause-related marketing, however, is not "image-oriented" as basic philanthropy is, it is distinguishable from such traditional approaches in that it is "bottom line-oriented" for the firm. Being bottom line-oriented alters several things for the firm involved in cause-related marketing. Two of the most prominent particularly stand out. First, from a practical standpoint, funds to support this type of activity should (and typically do) come from the firm's marketing budget. The firm that draws on its corporate foundation to support cause-related marketing activities is indicating a basic misunderstanding of the concept and intent of such activities. The impact that such resource allocation may have on the overall charitable activities of the firm is a questionable issue to those on both sides of the cause-related marketing fence.

Secondly, a bottom line orientation should alter the way in which cause-related marketing's success (or failure) is judged. Its intent is not solely to improve a company's corporate image (a rather nebulous objective that has proven difficult to measure for firm's engaged in philanthropic activities through the years). Cause-related marketing, instead, is designed with specific objectives related to increasing business for the firm (however that increased business is measured: sales revenues, number of customers, profits). In this regard it is easier to judge success since specific, quantifiable measures are present but it also puts greater pressure on the cause-related marketing activity to prove itself. As Higgins (1) points out, activities that do not have specific measurement criteria built in, activities whose objectives are to produce "warm and fuzzy" feelings toward the firm, are not cause-related marketing. Firms branding them thus are confusing marketing with publicity.

Having distinguished cause-related marketing to some extent from philanthropy and the basic charitable activities of a firm by exclusion, it would be helpful to define it in terms of what it is, rather than only what it is not. Cause-related marketing activities are activities of a private firm that directly benefit their business while simultaneously benefitting a chosen social or charitable cause. To be judged successful, both parties (the firm and the cause) must profit. A cause-related marketing effort that provides support to the named cause but does not benefit the firm by meeting the business objective specified for it must, by this definition, be deemed a failure. American Express, for example, promoted a project they called Project Hometown America. Each time a new American Express card was issued or an existing one used, a specified dollar amount went to a fund that provided dollars to a variety of grassroots social programs throughout the country. From a charitable view, the $4 million donated to social programs would certainly brand the program a success. From a business perspective, however, American Express reported only marginal increases in card usage and applications. By a cause-related definition, the activity was a failure.

Cause-related marketing can be further defined by looking not only at its relationship to the firm and the nonprofit or social cause but to the consumer as well. The concept, after all, is enmeshed in an intricate triangle with these three parties. Wiegner (2) describes the role of the consumer by stating, "give consumers an easy way to fill [their] altruistic desires by buying your product and you have 'cause-related marketing'". Cause-related marketing may indeed solve the age-old problem of nonprofits who find that a "good feeling" is simply not enough to offer in exchange to someone for a tangible contribution. When a consumer participates in a cause-related marketing activity, they can feel good about the contribution they are making to a cause while at the same time acquiring goods or services that provide them with a direct, tangible benefit.

As defined, cause-related marketing is a distinguishable activity from the charitable and philanthropic activities of a firm. Thus when critics such as Maurice Gurin (3) maintain that the basic concept of cause-related marketing is flawed because it fails to recognize the rationale for a philanthropic sector, they themselves are failing to recognize the distinction between philanthropy and cause-related marketing. The latter does not (and probably should not) replace the former, rather the two can and do co-exist, complementing each other, in many firms.

Benefitting the Public Sector?

The first issue of critical importance in judging the efficacy of cause-related marketing pertains to the nonprofit organization or social cause that is to profit from the effort. As defined earlier, both the nonprofit and the company must profit. If the nonprofit cause does not profit, the cause-related marketing effort is not a success. Profit, however, should be evaluated by means beyond solely monetary gain in this instance.

Does cause-related marketing help or hinder the nonprofit organization that is its target? At first this would appear rather obvious. How can the organization help but benefit from efforts undertaken by a corporation in its behalf? Any amount of money raised for the cause is a "profit" from the organization's viewpoint. But as pointed out above, monetary gain may not be the only issue of consequence here.

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The nonprofit might fairly raise the question of whether there will be "strings attached" to the efforts and contributions of the corporation. At a minimum, most corporations expect their name to be prominently displayed in materials associated with the cause. Nonprofits, for the most part, appear comfortable with this agreement. An organization such as the Tampa Symphony Orchestra no doubt feels that naming its pops concert series the Citicorp Super Pops is a small price to pay for sponsorship of the program by Citicorp (4). As such recognition grows more common, however, the public sector partner may feel increasing pressure to not only recognize the source of their support but to give it an increasingly prominent role in their promotions and activities. There may be no turning back as the nonprofit continues to accept dollars from the firm which in turn continues to overtake and overshadow the cause-based organization. While profiting monetarily, at some point the nonprofit may feel the cost outweighs the benefit and yet be unable to extricate itself.

On a contrasting note, it would be wise to question whether the nonprofit organization could be mistakenly lulled into believing that more is forthcoming from the organization than actually is the case. A sense of complacency may overtake the nonprofit who has established a symbiotic relationship with a corporation over a period of time. Since the cause benefits at the pleasure of the corporation, such a false sense of security could spell problems for the organization. A company that encounters problems cannot be counted on to continue its cause-related activities. The recent volatility of the stock market provides a dramatic example of uncontrollable factors that could have a chain effect on the cause being targeted.

While such indirectly non-monetary issues as the two just discussed must be considered in assessing the benefit of cause-related marketing to the nonprofit organization, the effect of such activities on the monetary position of the cause cannot be overlooked. It may seem nonsensical to question whether the $1.7 million generated for the Statue of Liberty by American Express or the $1 million raised by General Foods Corporation for the Muscular Dystrophy Association through couponing are beneficial to the causes in question. In looking at the larger issue of fundraising, however, the wise organization should question the impact that cause-related marketing activities may have on their overall ability to raise funds. Two potentially detrimental scenarios present themselves.

First, can the sponsoring corporations be counted on to clearly differentiate between their basic philanthropic activities and their cause-related marketing programs? As discussed previously, the two are not the same, they should complement each other, not substitute for one another. Furthermore, monies to support the two should come from two entirely separate places (charitable giving coming from foundations or other funds earmarked for community giving, cause-related funds coming from corporate marketing budgets). The corporation that views their cause-related activities as alternatives to generalized corporate giving, however, may in actuality be reducing their total contribution. This is, in fact, the basis of Gurin's (5) fear that "if cause-related marketing became widespread, it could undermine the very basis of philanthropy."

The second question the nonprofit should face is whether cause-related efforts could hinder their personal abilities to raise funds and other types of support. Corporate fundraising activities may meet with less and less success as the cause becomes increasingly associated with another firm. Furthermore, individual fundraising efforts could be hampered in two ways. First, by what Caesar (6) refers to as the "taint of commercialism." Donors, both companies and individuals, may feel uncomfortable giving directly to a private sector corporation. Many potential donors no doubt believe that nonprofit organizations and the public sector in general somehow remain "pure" and above the "dirty work" of the private, for-profit sector by maintaining a distance. Since cause-related marketing, by necessity, directly links the nonprofit and the corporation, such distance cannot be maintained. Could this discourage a potential donor from an act of direct giving? Potential donors may feel that the nonprofit's image is in some way "sullied" through its association with the products of a private firm. The nonprofit may be viewed as selling the products of the firm in some way thus raising the question of integrity. When General Foods raised money for school athletic equipment by sponsoring "Fun 'n Fitness" events linked to couponing efforts, they were criticized for turning school children into sales representatives for their products. (7)

Second, the risk exists that the cause may appear "well cared for" by the partner corporation. Potential donors may perceive that a cause is in less need of their support when it has been taken under the sheltering wing of a corporation engaged in a cause-related marketing activity. When Coca-Cola supported "Hand Across America," for example, with several million dollars generated through sales revenue, one can only guess at how many potential individual donors chose not to send a more modest contribution. After all, "my $10 can't be very important compared to what the cause is getting from Coke."

Should any of the above outcomes result in sufficient reductions in total fundraising dollars as to offset the funds generated from cause-related marketing, the nonprofit is not benefitting. Thus while cause-related efforts clearly have the potential to benefit the nonprofit, it cannot be automatically assumed that that is the only possible outcome.

Benefitting the Private Sector?

Since the proposed definition of cause-related marketing suggests benefit to the company as well as the cause, consideration of its efficacy must include attention to its effects on the firm. Furthermore, the extent to which cause-related activities benefit the corporation is clearly a key in determining their likely status (passing fad or here to stay) since marketing activities that do not meet the business objectives set forth for them are destined to pass on quickly.

With any marketing activity, the biggest danger to the firm lies in the simple criticism that it doesn't work. Beyond questions of ethicality and appropriateness lies this acid test of any bottom line-oriented activity. Cause-related marketing may sound noble and altruistic but since its objectives are meant to reach beyond the "warm and fuzzy" feelings inspired by image oriented efforts, its efficacy can be judged more specifically. If the profit or revenue objectives set for the effort are not met, it must be judged a failure. If continued cause-related efforts are deemed failures for a corporation it would make good business sense to question the value of continued efforts of a similar nature.

The potential dangers to the firm associated with cause-related marketing, however, go beyond just the acid test of its profit viability to the firm. Beyond not generating the desired revenues or profits, could cause-related marketing efforts actually damage the corporation, either image wise or in even more concrete terms? Choice of an inconsistent, inappropriate, or overly controversial cause could damage the corporation. It is important for the firm to carefully consider their target market, both demographically and psychographically, when considering the causes they choose to support. Sports sponsorship or cultural events may be appropriate for firms whose target markets are thusly oriented. A blue-collar, television watcher, on the other hand, may actually be demotivated to purchase a product when part of the proceeds are going to support the opera or ballet. Likewise, the firm that supports AIDS patients with proceeds related to its revenues may find objections from certain target markets.

Causes with more generalized appeals (Coca Cola's association with Hands Across America or American Express' support of the Statue of Liberty for example) may have less need to be concerned with the choice of a cause inconsistent with the interests of their target market. Scott Paper Company, for example, currently supports six national health agencies, all involved in helping children with special needs, with contributions based on the sales of their paper products. Entitled "Helping Hand," Scott's efforts are likely to generate only positive feelings from consumers, in addition to increased revenues and profits. A controversial cause, however, may cause problems for the corporation as a result of the negative feelings it produces. The company that supports high school family planning clinics with proceeds from sales revenues may soon find little to go to the cause and even less to meet their own profit objectives.

To allay this potential problem some corporations have turned to creating their own causes. American Express' Project Hometown America was just such an approach. It was a generalized fund designed to provide support to deserving local nonprofits on a national basis. Any such organization could apply for funds which were meted out at the discretion of American Express. To protect themselves from criticisms regarding choice of causes to fund, a board of volunteers from assorted nonprofit organizations was appointed to make funding decisions. Still American Express was backing the decisions and as Wiegner (8) points out, "Isn't there a risk that rejected grassroots groups will blame American Express if there's not enough money to go around?"

Here to Stay or a Passing Fad?

As we move toward the year 2000, the face of corporate philanthropy is changing. Firms, while still desiring to be socially responsible corporate citizens, are finding it increasingly difficult amidst the realities of today's financial market to remain strictly charity-oriented in all their giving programs. This is the environment that has paved the way for cause-related marketing. To the extent that the independent sector can aid corporations in adjusting their philanthropic endeavors to this changing environment, all parties involved stand to benefit and cause-related marketing could be predicted to root itself firmly in the corporate repertoire of marketing activities.

As can be seen from the discussion in this paper, however, the answer to the continuing efficacy of cause-related marketing is more complex than the above would suggest. While the veneer of such activities is clearly positive for the nonprofit sector, organizations in this sector must be warned to dig below the surface in analyzing the total impact such programs could have on them. It is easy to be dazzled by corporate promises of large sums of money, but the cause must be cautious. Consideration of the nature of the commitment and its likely long-term consequences on the cause are critical. The nonprofit should consider all potential consequences of the program as the first step in assessing an offer of such aid from a corporation.

A conscious decision to accept or reject the offer should be step two for the cause. This is important since there is always a temptation to say "yes" when money is offered. Such in-depth analysis will no doubt uncover occasional instances of cause-related activities that do not clearly benefit the nonprofit sector, however. These programs should be unhesitatingly rejected by the cause-based organization.

Despite the credo for the above two steps, it is likely that the nonprofit sector will frequently find it difficult to reject the offers of assistance that cause-related marketing programs dangle before them. It will be left, therefore, to the private sector to ultimately determine whether cause-related marketing is here to stay or not. Beyond all other considerations, the overriding issue for this sector, as identified earlier, will be, does it work? If it meets the goals of the firm, both in terms of their revenue and profit objectives as well as their social responsibility aims, it appears here to stay. While the final answer to this will come only with the test of time, it would appear that a concept with the clear cut potential to benefit all parties involved (the corporation, the nonprofit sector, and the consumer) while dealing progressively with a changing environment stands an excellent chance of being here to stay.

Notes

1. Higgins, 1986.

2. Wiegner, 1985.

3. Gurin, 1987; see also, Haugh, 1981 and Wiegner, 1985.

4. For additional examples, see Mescon and Tilson, 1987.

5. Gurin, 1987.

6. Caesar, 1986.

7. For a more thorough discussion of this, see Haugh, 1981.

8. Wiegner, 1985.

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WORKPLACE FUNDRAISING:
HOW CHANGES IN THE DONOR BASE, THE WORKPLACE AND NONPROFITS WILL EFFECT WORKPLACE CHARITIES AND THEIR SPONSORING EMPLOYERS

by

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Prepared for the 1988 Spring Research Forum
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Poor Richard Ferris. About a year ago, Mr Ferris was at the head of one of the most successful, admired and profitable businesses in America - United Air Lines. Then Mr. Ferris tried to double his base by creating Allegis Corporation, a conglomerate which included corporate luminaries such as Hertz, Conrad Hilton Hotels and other travel-industry giants.

It was the creation of this mega-business which eventually led to Mr. Ferris' undoing. By last Fall corporate raiders, jittery stockholders and financial forces beyond his control combined to drive Mr. Ferris off the top of the corporate mountain and shatter, probably forever, Mr. Ferris' dream of leading a corporation twice the size of United Air Lines.

But while all this was going on, Mr. Ferris had another concern. He was chairing the Strategic Planning Committee for United Way of America (UWA)'s Second Century Initiative - a committee which recommended to the UWA Board of Governors that it double its financial and volunteer capacity within the next five years.

Some people would say Mr. Ferris had a credibility problem.

But the real question for us here is whether UWA, under pressure from non-profit raiders, jittery stakeholders and social realities beyond its control, will be able to double its two most precious commodities by 1992.

If it can, UWA will not only have defied social and charity trends, it will also have defied its own and others' analyses of workplace trends.

If UWA cannot raise the money and the volunteers, few will be surprised and probably fewer will be deeply affected. But all of us who work with non-profits and who recognize the desperate need for more money and volunteers will be disappointed. Disappointed that the goal was not reached and saddened that a great American charity maybe driven off the mountain by pride

But before we get too far ahead of ourselves, let's talk a little about workplace giving - its history, why its so important, the charities involved, why corporations play such a key role and who the rest of the players are. Then let's lock at workplace, social and charities trends which may be impediments or opportunities for UW double its resources.

First, workplace fundraising is the joint effort of employers, employees and charity supporters to solicit annual pledges and cash gifts from employees during a 2-3 month campaign period.

The workplace solicitation system (aka payroll deduction drives) has its roots in labor union dues, war bond drives and Henry Ford's efforts to keep workers "on-the-line" without interruption from a plethora of in-plant solicitations.

The old Community Chests and their successor organizations, the United Ways (UW) were the first to effectively use workplace solicitation for a multitude of member charities. With the assistance of supportive corporate managers, scandals in health charities and exclusive arrangements with the AFL-CIO and the National Football League, United Way became "America's charity."

But in the 1960's John Kennedy opened the federal employees' Combined Federal Campaign to non-United Way charities, Walter Bremond opened the first Black United Fund in a storefront office in Watts and the civil rights, equal rights and anti-war movements opened up the minds and hearts of the American public to new definitions of charity.

These were the roots of the Alternative Fund movement. A movement which now includes over 100 non-United Way funds and foundations and which annually raises over $100 million dollars through workplace solicitation.

These Alternative Funds are comprised primarily of local coalitions of similar organizations such as national health agencies (Combined Health Appeals and National Voluntary Health Agencies), arts groups (United Arts Funds), social action organizations (Community Shares), colleges (United Negro College Funds) as well as women and minority owned/operated service and cultural groups (Black United Funds and Womens Federations).

$100 million is a lot of money for these organizations but it pales in comparison to United Way's combined 1987 receipts of over $2.5 billion. So why the fuss? Why do UW Campaign Directors lie awake at night worrying about a lot of little Funds whose combined receipts total less than 4% of United Ways?

Conversely, why do hardnosed neighborhood organizers join with supporters of the symphony; pro-lifers join with pro-choice forces; union officials join with right-to-workites for the opportunity to raise so little money with so much work?

Why the struggle for and against access to workplace solicitation campaigns? Four reasons which are all addressed in the Rockefeller Brothers Fund and Independent Sector's survey "The Charitable Behavior of Americans" :

1) According to the survey,[1] a major donor's primary motivation for giving to UW is the "deductibility from salary." According to the survey, payroll deductibility was three times the motivator of either "UW helps the poor" or "UW does good, reputable work."

2) According[2] to the same survey, the approaches most likely to elicit a donation were, "asked by someone you know well" and "asked to give at the workplace." The combination of these two approaches has proven to be a very effective fundraising tool for UW and other workplace solicitation charities.

3) With the exception of religion, the IS survey[3] found that proportion of repeat gifts was higher to UW than to any other well-supported charity including education, medical charities and international relief efforts.

4) Finally, the survey[4] also showed that there is a fairly direct relationship between giving and volunteer time. Although

there have not been studies conducted on volunteerism and Alternative Funds yet, nevertheless, employer-sponsored involvement in workplace solicitation campaigns seems to be a very effective means for recruiting volunteers who become loyal donors.[5]

You should know that there is another reason why workplace solicitation is such a battle ground. Although it's not supported by any surveys or studies, nevertheless the reason is obvious to those who remember UW's "one gift for all" promo campaigns.

In fact, a gift to UW was never "one gift for all" but UW used this line of reasoning to support its workplace monopoly and, as the promo becomes less and less true, so does the support for a monopoly solicitation and a monolithic funding mechanism.

Why are corporations at the heart of this struggle?

A) Because unlike government employers, Alternative Funds have few legal rights when pursuing access to private employees. All access to corporations such as IBM, AT&T, Apple Computer, EcoLabs, Apache Oil and Lotus Development have been gained through persuasion, the toughest battleground of all.

B) Because the per capita gift of federal employees (and most state and local government employees) hovers around $40. The per capita gift of employees who work for major corporation (more than 500 employees) is seldom less than $100.

C) In addition, to a higher per capita, private employers usually pay for or defray the costs of soliciting their employees through the direct assumption of campaign costs, contributed Loan Executives or corporate gifts which more than pay for the costs of campaigns.

D) Both UW and Alternative Funds actively develop private employers at both ends of the size spectrum. Large employers are "developed" to maintain/gain access to large gifts and large numbers of employees.

Smaller employers are solicited primarily because both UW's and Alternative Fund believe that's who most employees will work for in the future and because most small employers are not currently solicited by UW they are not as loyal to any particular Fund.

Both United Way planning reports and Alternative Fund access patterns indicate that small businesses will be the most hotly recruited employers during the next few years.[6]

E) Finally, corporations are at the thick of this struggle by choice. According to one United Way volunteer, "the United Way board of directors that doesn't look like a Chamber of Commerce board, is not a successful UW."

Regardless of their reason for being active in UWs, business leaders in affect, "own and operate" both local and national UWs. The decision to attempt to maintain UW's workplace monopoly is theirs and thus they are both Alternative Fund targets and antagonists. Or as one Alternative Fund leader put it, "both damsel and dragon." They couldn't be more at the heart of this struggle if they tried.

Who are the "players" in workplace solicitation?

We've spoken of the employers and of the federations/funds which gain solicitation rights from the employers.

Who's left? Two groups - employees and the charities who are assisted by the workplace solicitation federations/funds. It is these two groups - the donors and the donees - who are really the trend setters, who will really determine whether UW meets its 1992 goal.

So what are the trends for employees? According to predictions by officials of both UCLA and USC's Schools of Management, the following changes in employment will be commonplace by the mid-90's[7]:

- portable pensions
- flexible benefit packages
- entrepreneur centers within companies
- increased "self-management" (hiring, pay scales)
- increased use of flex-time
- concentrated employment on both ends (very large & small employers)
- equal number of women/male managers
- increased number of off-site/at home workers
- increased self-employment/contracted services
- increased level of middle-management

In short a trend towards increased options, increased individualism, decreased paternalism and decreased size.

In addition, surveys and voting patterns are already showing the following trends for workers outside of the workplace:

more managers who have been involved in non-traditional charities (civil/equal rights, anti-war, neighborhood self-interest)[8]

more emphasis on options in every facet of life - housing, profession, job structure, marital status and living/working sites.[9]

more flexibility in their view of community problems, political loyalties and approaches to community solutions. (In a recent election, California citizens swept out of office State Supreme Court justices who opposed the death penalty and at the same time overwhelmingly voted against an anti-AIDS victim referendum.)

more insistence on control over their futures - increased use of IRA's, increased technical education, increased use of personalized investment plans and less loyalty to one church.[10]

In short, a trend towards long-term solutions, towards self-help, away from authority and a tolerance of individual differences.

What about the target charities - the donees?

The major trend is just in the numbers. The Internal Revenue Service reports there are three times as many charities as there were just 20 years ago.

According to the Urban Institute, the financial picture of human service non-profits will be changing dramatically.[11]

Less dependence on a single funding source

More diverse income - both earned and unearned

Funding for innovation will diminish

A study for the University of Chicago concluded that social service agencies are increasing their dependence on earned income from wealthier clients (e.g. recreation programs in wealthier communities, programmatic re-focusing on the provision of psychotheraputic remedies as opposed to system change or "life opportunities".)[12]

But the same study suggested fewer poor people are using non-profit service agencies because of their inaccessibililty (location and hours), because of the specificity of the service and because of the tight eligibility standards.[13]

According to one charity review official, fewer charities are accepting traditional accountability and financial practice standards (e.g. fundraising/management cost under 30% of income) .[14]

At the same time, procedures and criteria for evaluating the value of programs are becoming more expensive and

less exacting. The value of traditional "headcounts" is thankfully being diminished but new procedures/criteria which evaluate the increasingly complex programs needed to overcome client/client group problems are not being developed.[15]

According to one source, there are over 4000 incorporated neighborhood organizations (not including Crime Watch groups) in the US.

One mailing list house indicates there are now 15,000 foodshelves and emergency shelter groups, over 3500 peace and anti-nuclear power/arms related groups, 1800 environment and wildlife related organizations, over 1000 community development organizations and 700 tenants unions. In the last two years alone, 32 organizations of the homeless developed.[16]

In short, broad changes in the financing of non-profits, a diminution of the traditional value of social service agencies for the needy, an increased number of non-traditional, self-interest self-help or advocacy charities and a major de-emphasis on traditional means of evaluating the worth or "charitability" of charities.

purposes.

How will these trends impact United Way's Second Century Initiative plan?

As befitting an organization which emphasizes consensus and de-emphasizes controversy or divergence, United Way does not seem to have developed a very clear picture of how it will handle these new trends.

Traditionally, UW has emphasized large centralized allocations systems, amelioration services and large traditional charities. It has emphasized one campaign and one workplace charity. How will it handle divergence, multiple charities, donor demand for choice and non-traditional charities?

So far the theory from the UWA seems headed in the right direction. The Second Century Initiative's implementation suggestions include more emphasis on flexibility, donor choice, expanding services and correcting funding inequities.[18]

There are passing disparaging remarks about the competition, controversy and the great need for a single campaign, but these maybe UWA's rough equivalent of saber-rattling for the troops on the frontline.

It is these troops on the frontline, the local UW Executives and Campaign staff/volunteers who make us wonder whether the national rhetoric of good faith will ever be implemented on a local level.

For at the same time UWA emphasizes flexibility, the Denver Mile High United Way sends nasty letters to employers who are considering a joint campaign for UW, a womens fund, health agencies and advocacy groups.

For at the same time, UWA emphasizes donor choice, UW of Cleveland sends memos to its staff telling them never to discuss donor option at the risk of their positions.

For at the same time UWA talks about expanding services, the only three organizations ousted by St. Paul and Minneapolis UWs are Black and Hispanic-operated community centers.

For at the same time UWA talks about correcting funding inequities, officials of the Seattle UW call the leader of a competing womens fund, "a radical lesbian separatist."

In the final analysis, whether UW achieves its goal of doubling its funding and volunteer base will depend on whether the national rhetoric or the local vitriol achieves the upper-hand.

If the local vitriol continues, neither UW nor its competitors will ever achieve the potential volunteer and financial support which American donors and employers have granted their charities in the past. An ever eroding public trust and tolerance will be the only legacy of such ill-will.

However, if the national rhetoric gains popularity and command

So for both employees and charities - donors and donees - we see some overarching themes:

A move towards self-reliance/self-control and away from dependence on system-based values.

A move towards many smaller groups and away from one force.

A move toward options and away from other-selected choices.

A move towards diversity and away from sameness.

What do the trends mean for the donor-donee arrangement?

A) Employees want a choice and they want to know that their money is sent to the charities for which it was intended.

B) Traditional "good" non-profit management may not carry the evaluative weight it once held for contributors.

C) Solutions are a critical value for contributors. Band-aids, except when it applies to the donor's immediate situation are of less value than many years ago.

D) Donors are willing to support a new, more controversy-based organization as a legitimate charity worth supporting (even if they disagree with the politics or program)

E) Large and well-known charities, will still carry clout and sympathy but will not necessarily be considered more "charitable" than smaller, localized, non-traditional groups.

What does this mean for workplace solicitation campaigns?

A) Although they may be less dominant traditional charities by virtue of their ability to present themselves often and without reproach, will continue to be the darlings of workplace solicitation campaigns.

B) Donors will accept less-traditional, advocacy groups

either in the umbrella of a UW or a more explicitly political federation.

They may not necessarily give to them but they will accept them.

C) As the Yale Program on Non-Profit's "Working Paper #93" suggests, employers will offer giving options to their employees as an inexpensive but attractive work benefit.

D) Both traditional and non-traditional charities will focus on their ability to solve community problems and to develop self-reliance.

E) Both will de-emphasize paternalistic giving practices and centralized allocation activities.

F) Both will continue to focus on donor choice while still maintaining some control over the donee groups for marketing on the local level, there is no doubt that UW, in spite of other shortcomings, will be the caring system it really wants to be.

But until the struggle for control of UW's soul has ended, perhaps Richard Ferris' own words will serve as both a caution to UW as well as an underlying raison d'etre for all workplace fundraising efforts, both United Way and its competitors - the Alternative Funds.

In his opening remarks to "Rethinking Tomorrow and Beyond - Some Thoughts on the Continuing Evolution of United Way As A Responsive and Inclusive Community Caring System" , Mr Ferris and his co-author, James Robinson write: [19]

> "We cannot improve upon United Way's mission: 'To increase the organized capacity of people to care for one another. But we can become more effective at achieving that mission by tapping new resources and by enhancing our capacity."

If Mr. Ferris and the other the corporate executives who direct the future of United Way really want achieve UW's goals and truly increase our capacity for caring - they will drop their shrill cries of "donor raiding", forego their claims to employee monopoly and come down off the mountain. In so doing, they will have achieved more than just one non-profit's goal. They will have also attained the quintessential American goal - "E Pluribus Unum" - "From Many - One."

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WORKING DRAFT

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CORPORATE CONTRIBUTIONS TO THE YEAR 2000: IS A SLOWING OF GROWTH INEVITABLE?

by

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The meteoric growth of corporate charitable contributions in recent years has captured the attention -- and the imagination -- of the entire philanthropic community. That any private source of funding could, and would, triple its giving in only ten years, as corporations did between 1976 and 1986, has inevitably thrust the subject forward into the limelight.

The excitement engendered by the rapid growth of corporate giving after 1975 also generated much interest in the long term prospects. Could one realistically expect continued growth at annual rates of 10 percent or more indefinitely, or at least to the year 2000? Or would there inevitably be a secular slowing to a lower rate, and if so, what rate?

The answers to these questions constitute the subject of this paper. In a nutshell, this author believes that the growth of corporate contributions in the future is almost certain to be much slower than in the past. Which is not to say that corporate giving will decrease, or that it will flatten out, or that it will not show short-run spurts of rapid growth. But, given reasonable assumptions about economic activity, inflation, the tax laws, and similar influences, a decline in the average rate of growth is almost inevitable. Indeed, it may already have begun.

While it will be several months before we have any real clue as to what happened in 1987, and more than two years before we have complete figures, it has been clear for some time that the growth of corporate contributions has slowed down appreciably since 1984. The average annual increase amounted to 14.4 percent between 1975 and 1984, but the available estimates indicate that growth fell far short of that figure in 1985 and 1986, and there may even have been a slight decrease in giving last year.

The prospects for this year, 1988, are by no means clear. Some fragmentary information about the intentions of a few of the major corporations suggest that there will be a modest increase, but there is an unusually high degree of uncertainty in the picture arising primarily from economic and political factors.

However, our concern is not the immediate future but the long-term future, to the year 2000 and perhaps beyond. And our subject is corporate contributions, not corporate philanthropy. Despite the fact that there are at least two newsletters and one book with the title Corporate Philanthropy, and despite the fact that the term is widely used in other ways, the reality is that there is no such thing.

I think that the question is important. The names we call things ought to be descriptive of what they are, they ought not to confuse the issue, and they should convey as accurate an image of what we are talking about as is possible. Even more important is the tendency to attribute something to a phenomenon that is implicit in a mistaken name. This is especially true of a term like "philanthropy."

Corporate contributions are not altruistic. Unlike private foundations, corporations exist for quite different purposes than that of giving money to charity. That many (but not all) corporations do give to charity is merely a reflection of the fact that many senior corporate executives believe that the self interest of their companies is served by doing so. And there are some corporate managers that accept the view that the corporation has a duty to do so. These matters will be discussed in more detail at a later point in this paper; for the moment, let us understand clearly that philanthropy is not our subject.

Having gotten the matter of terminology out of the way, I want to turn to the theme of this essay: the future of corporate giving.

A projection based on past growth.

The question is not so much quantitative as qualitative. If one were to deal only with the numbers, there would be little to say. The future is always an outgrowth of the past and this is especially true of all time-series data which measure economic phenomena.

For example, total corporate contributions — as measured by the amounts claimed on corporate tax returns -- grew from $30 million in 1936 to an estimated $4.5 billion in 1986. The implicit growth rate for this half century works out to roughly 10.5 percent per year. Assuming that corporate contributions continue to grow in the future at about the same average rate per year as in the past, then the figure for the year 2000 would be $18.3 billion. We could, of course, use other pairs of years and obtain different projections; between 1946 and 1986, for instance, the growth rate averaged about 8 percent per year and the projection to the year 2000 would be $13 billion.

As a guidepost to the future, these kinds of projections are only marginally useful because they beg the question about the forces that caused corporate contributions to grow as they did in past, and they shed no light at all on the influences that are likely to be important in the future. The only sure bet is that between now and the year 2000 events will not be quite the same as they were in the past.

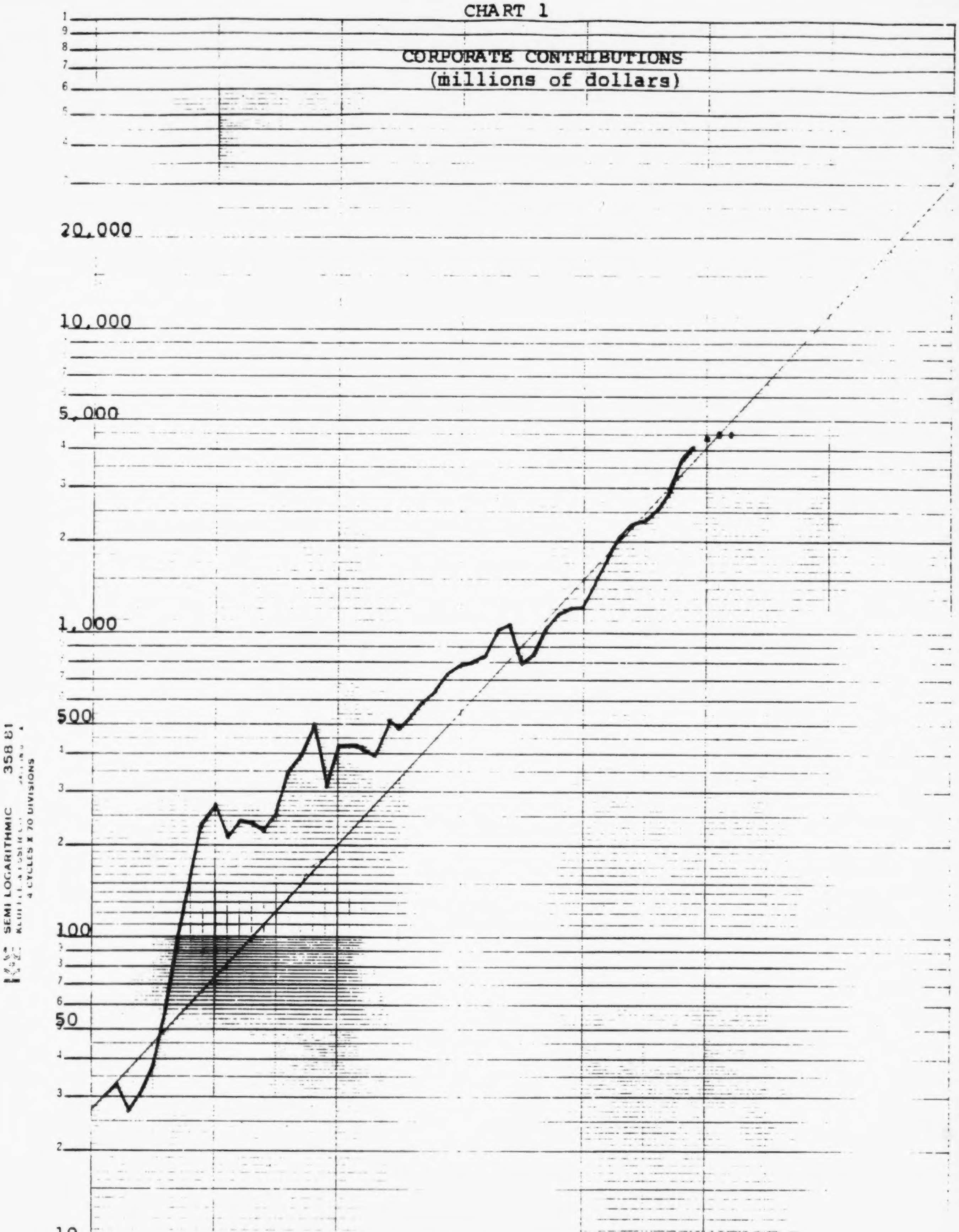
What can we say about all the things that caused corporate contributions to increase at 10.5 percent per year in the last half century? The question is important as well as interesting, because any useful speculation about the future of corporate giving requires at least some understanding of the history of such giving in the past.

A look at the record - in quantitative terms.

Chart 1 traces the history of corporate contributions from 1936

CHART 1

CORPORATE CONTRIBUTIONS
(millions of dollars)



to 1984, with estimates for 1985, 1986, and 1987. Also shown is the 10.5 percent growth curve connecting 1936 and 1986, with an extrapolation to the year 2000. It should be noted that the chart is semi-logarithmic, i.e. equal vertical distances represent equal ratios, not equal amounts (which is why the 10.5 percent growth curve is a straight line).

The first fact that hits the eye is that the growth of corporate contributions has been episodic; there are clearly evident four distinct periods of growth, the first three of which were followed by a decline and/or plateau:

	Growth	Decline & Plateau
1.	1939-1945	1945-1950
2.	1950-1953	1953-1960
3.	1960-1969	1969-1975
4.	1975-1986(?)	1986- (?)

The timing is fascinating. The first period of growth was coincident with World War II and the second period was coincident with the Korean War. It does seem likely that something associated with the two wartime periods had a positive impact on corporate giving, but it is not at all obvious what it was. Nor is it obvious what caused the third and fourth growth periods. And what about the periods of decline and plateau? Were they merely the aftermaths of conditions that ceased to exist or were they triggered by some negative influences?

The second fact that is evident from the chart is that the average annual rates of growth were typically greater than 10.5 percent for periods ending prior to 1969. While it is not unusual for any series of economic data beginning from a low base to show this kind of pattern, this chart offers evidence that the earlier growth of corporate giving was intrinsically more robust in certain ways than was the later growth.

Indeed, 1969 seems to mark a discontinuity between two periods, the major difference between them being the degree of stability. The one prior to 1969 displays a high degree of instability while the one after 1969 is unusually stable; in fact, the growth of corporate contributions after 1969 conforms to the 1936-1986 curve itself. Is this an accident or was there something in the picture that was different before 1969 than it has been since 1970. Some exploration of this is clearly in order.

One final observation about the graphic display of corporate contributions. As to the period 1975-1986, there is some suggestion of two subperiods — 1975-1980 and 1981-1986 — with similar characteristics. Both of these subperiods show a typical pattern of diminishing growth after the first three years, but unlike the prior history of corporate giving, there was no decline after 1980, at least through 1984 and probably through 1985 and 1986. It is as though the years after 1980 were given a new burst of energy. This, too, needs to be explored.

The qualitative story.

While the numbers are interesting and important, it is the story behind the numbers that is the most interesting and the most important. The history of corporate giving is actually a fascinating story, in part because so much was compressed into a comparatively short time and in part because it illustrates the interplay of the many influences at work in this area. In particular, we need to take a close look at the relationship between corporate taxation and corporate giving.

Toward the end of 1935 Congress amended the Internal Revenue Code to include, for the first time, an explicitly allowable deduction for corporate charitable contributions. Before then, some corporations did make gifts which, for tax purposes, they deducted as "ordinary and necessary" business expenses. Such deductions were challenged by IRS auditors, and many such challenges wound up in the courts. Ultimately, the courts evolved a benefit-based test; if the contribution bestowed a direct benefit on the donor, it was deductible, otherwise it was not. The 1935 Act put an end to this litigation by making all corporate charitable contributions deductible up to a limit of 5 percent of taxable income.

This change in the tax law initially had little effect on total corporate giving. There are no authoritative figures for 1935 and earlier years, but for the first four years after the passage of this legislation the amounts reported on corporate tax returns hovered around $30 million, or just under 0.50 percent of corporate profits before taxes. In the circumstances then prevailing, the tax treatment of contributions does not appear to have been a controlling factor.

This changed dramatically after the outbreak of World War II. In addition to increased ordinary tax rates, corporations became subject to excess-profits taxes. The result was that the marginal tax rate imposed on many corporations exceeded 80 percent. When faced with rates of this magnitude, additional charitable giving became very attractive because the after-tax cost was less than 20 cents per dollar of contribution. Given this incentive, and given the appeals of wartime charities, the corporate community increased its giving substantially.

The tax picture also gave impetus to the notion of "stockpiling" money in the hands of corporate-sponsored private foundations as a hedge against periods of poor profits. Indeed, many of the largest and most well known of today's corporate foundations were created in this era, in large part because of the attractiveness of financing them cheaply.

The end of the war and the end of the excess-profits tax saw an end to the sharp growth of corporate contributions. The pattern, however, was repeated in the early 1950s during the Korean War: another excess-profits tax, another upsurge in total contributions, and another spurt in the formation of corporate foundations. Clearly the imposition and removal of excess-profits taxes had much to do with the fluctuations in the level of corporate giving in the years between 1941 and 1954.

There were, of course, other factors at work that were specific to the periods, such as the appeals of war-related charities and the compelling needs of many nonprofit agencies that focused on social problems peculiar to the times. In addition, the military conflicts generated increases in corporate profits, both before and after taxes, that were broadly parallel to the changes in corporate giving, and it seems clear that there was at least a rough causal connection between them.

Nontax influences.

One can only speculate what the course of corporate contributions would have been in the absence of wartime conditions and excess-profits taxes. There is, however, a clue in the behavior of contributions expressed as a percentage of profits before taxes in the peacetime years. Between 1936 and 1941, this figure was typically less than 0.50 percent. From 1947 to 1950 it averaged just under 0.70 percent, and from 1954 to 1960 it averaged close to 0.90 percent. Assuming these to be "normal" years, it is clear that there was a slow upward trend in the importance of charitable giving relative to profits.

What forces caused this upward trend? The most satisfactory analysis of which this author is aware concerns the evolution of the climate of opinion prior to the late 1960s.

Three obstacles and how they disappeared.

Going back to the 1930s, there is much evidence to the effect that it was then not considered proper for corporations to be involved in eleemosynary activities of any kind. The business of business was business, not charity and not action in the social sphere. Moreover, there were three fairly distinct obstacles to the willingness and ability of corporations to undertake any involvement in social matters. 1/

The first was legal. A judicial dictum handed down from one of the British courts stated that "charity has no seat at the Board table." 2/ As the managers of corporations had become increasingly divorced from the ownership, they were more and more regarded as the custodians of the property and other resources belonging to corporate stockholders, and they had no right or authority to distribute funds which they did not own themselves for the support of charitable enterprises. Indeed the powers derived from corporate charters did not include charitable giving, and, prior to the 1930s, only a few states had amended their corporate statutes to include contributions as a legitimate activity.

The second obstacle arose from the teaching of classical economics. In this view, the ability of a corporation to make gifts to charity was clear evidence that the corporation was at least a quasi-monopoly. In the theory of perfect competition, each of factors of production (land, labor, and capital) would be paid only what was required to get the amount that would be needed for the enterprise, no more. If the corporation had any surplus for charitable giving, it was confessing to an exploitative influence over prices that it was not entitled to have. Corporate management must have felt especially uncomfortable on this score when Congress set up the Temporary National Economic Commission in the late 1930s to investigate the market structure of the leading industries.

Finally, there was another reason why it was felt that corporations should not indulge in eleemosynary kinds of activity, one that involved the concept of welfare. Whether it was education or any other field of charity, social involvement was thought to be the function of individuals, churches, and government; not business. In theory at least, corporations could be accused of encroaching on the prerogatives of government and other sectors if they moved into any welfare activities.

This was the position in the 1930s. While it continued to characterize some corporate thinking for many years, the force of these three obstacles eroded steadily. By the early 1960s, the dominant view in all three areas was exactly the reverse of what had been the case only a quarter century earlier.

On the legal front the circumstances had changed completely. By 1960, nearly all the states had adopted statutes expressly empowering corporations to make charitable contributions. And the issue had been tried successfully in the courts, with the result that legality was no obstacle at all. Indeed, in the landmark case in the early 1950s, the court ruled that corporations not only had the right to make contributions, they also had a duty to do so as a matter of social responsibility. 3/

Likewise, the classical economists' model of perfect competition gave way to a more sophisticated view of the proper structure of business. Some degree of monopoly power seemed an acceptable price to pay if business would better serve the interests of society through large-scale production, mass marketing, and mass consumption. Modifications of perfect competition became accepted as a means of stimulating the development of new ways of doing things and rewarding initiative and enterprise.

As to business participation in welfare activities, the older view gradually disappeared, and in its place there grew an awareness that the business community is perhaps the most effective device in our society to get things done. The inability of government and other sectors to accomplish all the things that society wanted done led more and more to the notion that the help of corporations should be sought in areas that were formerly off limits to business. Today we hear of the creative interface between business and the rest of society, of partnerships between business and government, and of community initiatives involving corporations.

In retrospect, it seems clear that these changes were the dominant forces behind the growth of corporate contributions prior to 1970. The two wartime periods with their associated changes in the tax law were merely a kind of overlay to the fundamental trends. Corporate giving as a percentage of corporate profits was clearly increasing. In the ten years after 1960, it averaged nearly 1.07 percent and was below 1.0 percent in only two of the ten years; prior to 1960, it was as high as 1.0 percent in only three years and they were all in wartime.

Again, the matter of taxation.

While there is now an impressive body of evidence that tax policy does have an influence on the propensity of individuals, especially those in the upper income groups, to give to charity, no one has ever investigated the relationship between taxes and corporate contributions. Yet it is apparent that the imposition of excess-profits taxes did have an important influence on corporate giving on the two occasions mentioned above. The liklihood that tax policy does play a significant role in corporate giving is reinforced by two episodes in more recent years.

A glance at the chart showing the history of corporate contributions indicates clearly that 1968 and 1969 were unusual years; there was an increase of more than 21 percent in 1968 and an additional small increase in 1969, followed by a 24.4 percent decrease in 1970. Relative to corporate profits before taxes, contributions increased from 1.04 percent in 1967 to 1.13 percent in 1968 and then to 1.22 percent 1969, the highest level since 1945. In 1970, the figure fell back to 1.06 percent.

The only factor that can conceivably account for this abberation in the growth pattern is the change in federal taxation in those years. In 1967, the Congress added a temporary 10 percent surcharge to both individual and corporate tax rates for 1968 and 1969; the surcharge fell to five percent in 1970 and was eliminated thereafter.

Again, as in the two wartime periods, there was not only an upsurge in corporate giving but also a spurt in the rate of formation of corporate foundations. The latter phenomenon was followed by a significant drop in 1970 and later years as a result of the Tax Reform Act of 1969 which, among other things, imposed stringent rules on, and a tax on the net investment income of, all private foundations, thus making such entities less attractive as vehicles for corporate giving.

The second episode is of current vintage, and it bears on the question raised earlier about the 1981-1986 subperiod. Prior to 1970, corporations could make contributions of company products (inventory) and claim a tax deduction based on fair market value. The basis for valuation was reduced to cost by the Tax Reform Act of 1969. Although there are virtually no data available regarding the total amount of these kinds of contributions before 1982, it is believed that such giving decreased sharply in 1970 and stayed relatively low until after 1981.

The tax treatment of gifts of company products has been changed twice since 1969, in both instances to permit a much more generous deduction, but only in special cases. The first change, in 1976, was designed to encourage giving to agencies providing care to "the ill, the needy, and infants." The second change, in 1981, was aimed at encouraging contributions of scientific property used in research.

In both instances, the new incentive for making contributions of inventory was effective. While it is clear that there was some growth in giving aimed at "the ill, the needy, and infants" after 1976, the amounts appear to have been small in comparison to total corporate contributions. The effect of the 1981 Act was much more dramatic, although valuation problems make it difficult to measure precisely. For example, gifts of company products reported by 1,194 colleges and universities in academic year 1985-86 amounted to $231 million,4/ and this figure understates the actual amount: $205 million was reported by only 69 companies in 1986.5/ Hence, a significant share -- perhaps as much as 10 percent -- of total corporate giving is now made up of gifts of company products.

The Economic Recovery Tax Act of 1981 also raised the limit on the charitable deduction for corporations from 5 to 10 percent of taxable income. The long-term effect of this change has yet to be determined, but it clearly had a significant impact in 1982. There was a 22.4 percent increase in the number of companies reporting contributions equal 5 percent or more of net income and a 38.4 percent increase in the average amount of their contributions. The contributions of companies reporting 5 percent or more increased from 25.5 percent of total giving reported by all corporations in 1981 to 37.7 percent in 1982.6/ There are technical reasons why the amounts reported for tax purposes may not be the same as the amounts actually given, but these figures suggest very strongly that this change in the tax law did have a positive impact on corporate giving.

To a very large degree, therefore, the reacceleration of the rate of growth of corporate giving after 1981 was induced by these two changes in the tax law. This episode strengthens the general view of taxes as an important influence on corporate contributions. There is likely to be some further influence as a result of the Tax Reform Act of 1986, but the provisions of that Act are not yet fully effective and there will be a time lag in the availability of data with which to appraise its impact. More on this subject later.

The climate for corporate giving.

However important taxation may be as an influence on corporate contributions, it is surely nothing more than a marginal factor that induces increases or decreases in the amounts given. Taxes alone do not appear to be a determinant of the decision to give or not to give. That decision is very clearly a function of the attitudes of corporate managers to the prevailing climate of opinion. We have seen how that climate and those attitudes changed between the late 1930s and the late 1960s. What can we say about them after the early 1970s and on into the future?

At this point we need to introduce three things. One relates to the incidence of corporate contributions, i.e. the distribution of the corporate population with respect to charitable giving. The second is the matter of inflation as it bears on corporate contributions. The third is the influence of corporate profits.

The incidence of corporate contributions.

The corporate universe is anything but static. Between 1970 and 1982, the number of firms filing federal tax returns increased from 1.7 million to more than 2.9 million. Some of the increase in corporate contributions was due not to increases in average levels of giving per company but to the growth of the corporate population. How much that population will grow between now and the year 2000 is unpredictable in the absence of any analytical framework, but any growth at all will continue to be a plus factor in the growth of corporate giving.

However, only a small fraction of the corporate community reports any charitable giving for tax purposes. In 1970, the first year for which we have any data on this subject, just under 20 percent of all corporations filing tax returns in that year reported any contributions.7/ By 1977 this figure had increased to 23.4 percent, but in 1982 it had fallen back to only 20.8 percent.[8] One may infer from these data that the rapid growth of corporate contributions between 1970 and 1982 was attributable to only about one-fifth of the expanding corporate universe.

That such a small fraction of all corporations report contributions for tax purposes is not surprising. Among the firms not reporting any contributions, well over half are net loss companies and virtually all of the others are very tiny enterprises. Since the tax law limits the charitable deduction to a percentage of taxable income, a net loss corporation may not legally report any contributions as a deduction for tax purposes. And the small firms with taxable incomes that report no contributions are really proprietorships or partnerships, not the kind of public corportions we think of in terms of charitable giving, and their owners normally give as individuals rather than through the companies they own.

It seems very unlikely that there will be much of an increase in the incidence of corporate giving in the future. There is likely, however, to be some increase in the corporate population, a corresponding increase in the number of companies reporting contributions, and a continued increase in the average amount of contributions per company.

The period for which we have this kind of data is relatively short, but it is worth examining as a possible clue to the future. In the 12 years between 1970 and 1982, there was an 83.9 percent increase in the number of contributing companies and an increase of 98.4 percent in their contributions average.[9] These factors underlie an increase of nearly 265 percent in total corporate contributions:

	Total Contributions (thousands)	Companies Reporting Contributions	Average
1970	$ 797,029	330,532	$ 2,411
1977	1,791,244	525,122	3,411
1982	2,906,463	607,700	4,783
Percentage increase, 1970-82:	264.7	83.9	98.4

Similar data for the years after 1982 are not yet available, but the continued growth of total contributions undoubtedly involved further increases in both the number of contributing companies and the average amounts reported for tax purposes. If the rates of growth for 1970-1982 were to continue to the year 2000, then the number of contributing companies would increase to 1.5 million, their average contributions would be $13,350, and total corporate contributions would reach $20 billion.

It is, however, unlikely that the 1970-1982 rates of growth will continue, especially for the contributions average per company. The actual 1970-1982 increase took place during a period of high inflation; on an inflation-adjusted basis, the contributions average per company decreased 20.2 percent in this period. We need to take a look at the way in which inflation impinges on contributions figures.

The effect of inflation.

The growth of average contributions, for companies that reported contributions for tax purposes, was 5.9 percent annually between 1970 and 1982; the rate of inflation during this period was 7.9 percent. It thus appears that real average contributions declined by about 2.0 percent a year. This does not necessarily mean that average contributions would have decreased by this much if there had not been any inflation; we really don't know what would have happened to corporate giving in the absence of inflation. Nor does this mean that individual companies, on the average, reduced their giving in real terms between 1970 and 1982; this result may well have arisen, at least in part, by a shift in the distribution of corporations as between large and small givers.

But this does suggest that much of the long-run growth of corporate contributions has been exaggerated by the upward movement of general price levels during these years. It is, therefore, useful to look at the data with an adjustment for rising prices.

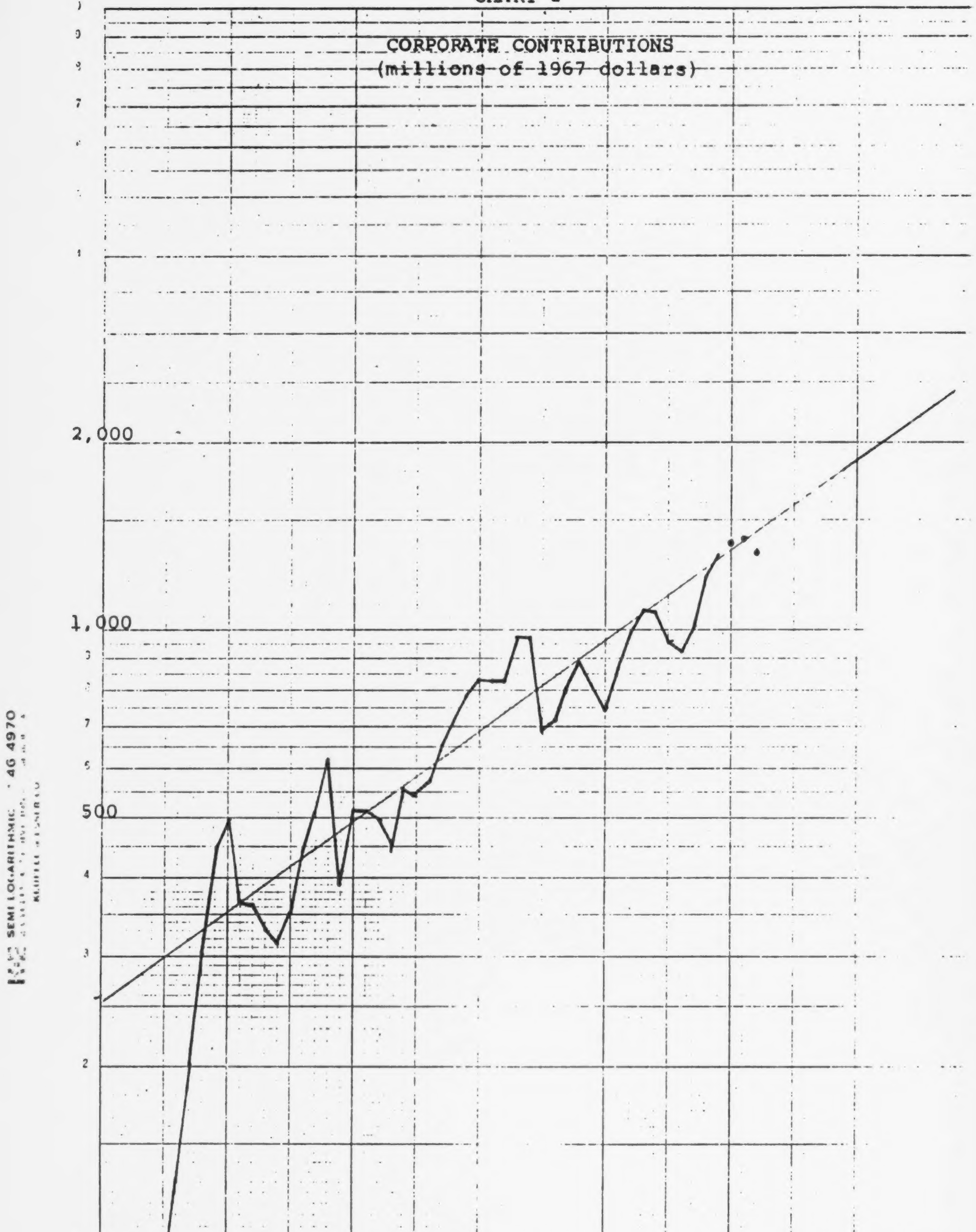
There exists no price index that is well suited for the kind of adjustment that is required. There is no price index that measures the purchasing power of the corporate profits from which contributions are made, and there is no price index that measures the purchasing power of funds put to charitable uses. The Consumer Price Index (CPI) is only a surrogate; but, on the positive side, it does measure in a very rough way the degree of inflation over a period as long as 50 years.

For the period from 1936 to 1986, the CPI increased at an average annual rate of 4.2 percent. This means that total corporate contributions increased not at the 10.5 percent rate that the unadjusted figures show but at 6.1 percent per year in real terms. When compared to other indices of real economic activity, this is an impressive rate of growth. For example, the gross national product (GNP), in constant dollars, grew only 3.6 percent per year, and corporate profits before taxes grew only 3.1 percent per year, in this period.

When adjusted for inflation, using the CPI to deflate the data to dollars of 1967 purchasing power, the historical picture of corporate contributions takes on a somewhat different complexion. These data are shown on Chart 2 for the period from 1941 to 1984, with estimates for 1985, 1986, and 1987. All of the data points for years prior to 1943 lie so clearly outside the pattern that they are irrelevant to further analysis.

For the years from 1943 onward, the data appear to conform to a well-defined trend, one that has an implicit growth rate of 3.4 percent per year (as against 2.9 percent per year for the GNP). This curve is shown on the chart, and an extrapolation to the future yields a figure of nearly $2.2 billion for the year 2000. Translating this number from 1967 dollars to 1987 dollars, the result is $7.4 billion. This may be interpreted as a projection of corporate giving from 1986 to the year 2000 based on the historical trend and the assumption of zero inflation. The actual number will undoubtedly be larger than $7.4 billion depending on the degree of inflation that occurs during the next 12 or 13 years.

CHART 2



CORPORATE CONTRIBUTIONS
(millions of 1967 dollars)

In passing, it should be noted that, with a projection of 3.4 percent per year in real terms, corporate contributions can continue to grow at 10.5 percent per year in current dollars only if inflation should average some 7 percent per year during the next dozen or so years. Whether that will happen, and if it does what its effect will be on corporate giving, is purely a matter for speculation.

The constant-dollar plot of corporate contributions accentuates the instability of corporate giving throughout the period shown. It also provides new insight into the developments since 1970. These data show, for instance, that corporate giving, in real terms, actually declined in 1974-75 and in 1979-81, something that one might have expected in view of the business cycle developments of those periods. These data also show that corporate contributions made a significant recovery after 1981, one that is most surprising in view of the sluggishness of corporate profits before taxes in recent years.

The influence of corporate profits.

Indeed, since 1979 the relationship between corporate contributions and corporate profits before taxes has taken an unprecedented turn. In all the previous periods for which we have data, corporate giving has mirrored in some degree the ups and downs of corporate earnings. The relationship has often shown a lag of a year or more, but by and large it has been remarkably stable, at least from the early 1950s to the early 1980s. Throughout the period 1952-1980 (with the exception of 1953, 1968 and 1969, for reasons indicated above), corporate contributions never amounted to less than 0.81 percent, or more than 1.10 percent, of profits before taxes. As noted earlier, there was an upward secular trend within this range.

Beginning 1980, however, the historical relationship changed in a significant way. Corporate profits before taxes declined in 1980 and remained well below the 1979 level for seven years, i.e. through 1986. Contributions, by contrast, rose in every year and by 1986 were nearly double their 1979 level. As a result, contributions rose from 0.89 percent of pretax profits in 1979 to an estimated 1.94 percent in 1986. Preliminary indications are that there was a sharp rise in pretax profits in 1987 while contributions were relatively stable, with the result that the percentage fell to about 1.60. This level is substantially higher than that for any year prior to 1982.

The percentage relationship for the last six years represents such a significant discontinuity in the historical trend and has such important implications for the future, that it requires a close look (see table on page 12).

An inspection of these figures indicates clearly that the discontinuity took place in 1982 and it reflected both a large increase in contributions and a sharp fall in profits before taxes in that year. In 1983 and 1984, there was a recovery in profits but there was a parallel further increase in contributions, with the result that the percentage did not change very much. Although the data for 1985-1987 are estimates based on surveys and other information, the probable errors are so small that the percentages are within a reasonable range of their true values.

	Corporate Contributions (millions) a/	Corporate Profits Before Taxes (billions) b/	Contributions as Percentage of Profits Before Taxes
1979	$ 2,288	$ 257.2	0.89
1980	2,359	237.1	0.99
1981	2,514	226.5	1.11
1982	2,906	169.6	1.71
1983	3,627	207.6	1.75
1984	4,057	240.0	1.69
1985	4,400e	224.8	1.96
1986	4,500e	231.9	1.94
1987	4.400e	275.0e	1.60

e = estimate by Council for Aid to Education

a/ Internal Revenue Service. Reflects amounts claimed as deductions on corporate tax returns; hence, these figures include amounts given to corporate foundations and exclude the grants made by corporate foundations.

b/ U.S. Department of Commerce

There has been considerable interest in this development. What are its underlying causes? Why should there be a sudden discontinuity in a relationship that had been so stable for so long a period of time? And, more importantly, what are the implications for the future? Will the relationship remain in the 1.60-2.00 percent range, will it drift back to its prior levels, or might it increase further in the years to come?

Four factors come together.

Adequate answers to these questions can only be conjectural in nature. Yet there are several known developments in these years to which one can point as contributing factors. None of these by itself provides a sufficient explanation of this extraordinary upsurge in corporate giving in the face of sluggish corporate earnings. Taken together, however, they suggest that to a very large degree the 1979-86 "explosion" in corporate contributions was accidental in the sense that several nonrecurring factors came together at about the same time. There are four such factors that can easily be identified:

(1) The changes in the tax law in regard to corporate contributions. As discussed earlier, the Economic Recovery Tax Act of 1981 (ERTA) raised the allowable deduction for corporate contributions from 5 to 10 percent of taxable income, effective in 1982, and it provided an enhanced valuation for the deduction of certain gifts of company products. The increased percentage limit has resulted in increased amounts of contributions reported by thousands of small, privately-owned corporations, in part because ERTA also lowered the marginal tax rates for individuals so that in many instances it became more advantageous for the owners of small

businesses to make their contributions through their companies instead of doing so as individuals. The upsurge in gifts of company products is now well known, and the available measurements indicate that the amounts are significant. Taken together, these two changes in the tax law may well have accounted for more than a third of the increment in corporate giving between 1981 and 1987.

(2) Gifts of surplus corporate assets. From time to time over the years, corporations have given surplus property -- land, buildings, equipment, etc. -- to charitable organizations, and the tax law provides a charitable deduction for such gifts. The valuation rules are complex, but essentially they allow a deduction based on fair market value with an offset for recaptured depreciation. This formula provides important incentives for the contribution of such property to charity once it is determined to be surplus to corporate needs.

By definition, these gifts occur randomly, and large gifts of this type -- say, $5 million or more -- were infrequent prior to 1982. In the last five years, however, and in large measure as a result of the massive restructuring of American business, ten or more such gifts in the range of $10 to $100 million are known to have been made. Taken together, these large, nonrecurring gifts account for a significant share of the 1981-1987 increment in corporate giving.

(3) Reduced government spending on social programs. One of the hallmarks of the Reagan administration has been a policy of trying to shift responsibility in the social sphere from the federal government to the private sector. In his 1981 budget message, for example, the President proposed cutbacks of several billions of dollars in federal social programs, saying at the time that corporations and foundations should take up the slack. The policy also manifested itself through the continued encouragement of local, private initiatives involving partnership arrangements in many of which corporations were expected to play a major role.

One of the consequences of this policy was a significant rise in the degree of attention given to corporations as funding sources by charitable organizations. Most of the larger, public corporations and their sponsored foundations experienced very significant increases in the number of requests for funding, a large part of which came from organizations outside the areas to which corporations had traditionally made their contributions. And most charities, new and old, became more sophisticated in their approaches to corporations. Although it would be difficult to measure the extent to which this pressure caused an increase in corporate contributions budgets, there is little doubt that the business community became more aware of, and responsive to, the increased needs of the charitable community. Some of the 1981-1987 increment in corporate giving is undoubtedly attributable to this development.

(4) Other changes in the climate for corporate giving. Accompanying the above developments were a series of changes in attitudes toward corporate giving, both internally and externally. Concurrently with the disappearance of the three obstacles to corporate giving between the late 1930s and 1970, there emerged two positive influences that slowly diffused through most of the corporate community. The first of these

was the concept of "enlightened self interest," and the second was the notion of "corporate social responsibility." The first involved the idea that corporate charitable giving was a permissable activity because it advanced the company's own welfare; the second went further by saying that the corporation has a duty to participate in efforts to solve social problems and to advance the welfare of the nation by making money, facilities and employees' time available to the charitable community.

By the end of the 1970s, the business world had begun to respond to these forces by moving contributions and related functions from an obscure corner of corporate life to a position of visability, from an incidental activity on the part of people whose principal duties lay in other areas to a very businesslike operation. The techniques that had proven so successful in other areas of the corporation were applied to contributions and other facets of corporate social responsibility, and the people involved increasingly brought a degree of professionalism to their work. Managerial philosophy also changed; instead of merely giving in reaction to the appeals for funds, the process became pro-active, with sets of objectives, budgetary priorities, planned programs, coordination, and accountability.

Externally, there was a growing awareness of corporate contributions and a rising tide of public expectations. It was more than that; in the early 1980s corporate giving was suddenly "discovered" as a new and untapped source of private sector money. Almost overnight, corporate contributions became the focus of interest in the philanthropic community, in the media, and among public officials. For example, the Council on Foundations, the Independent Sector, and other organizations turned their attention to this area and began to devote a substantial part of their program activities to it. The White House sponsored a Task Force on Private Sector Initiatives and the Business Roundtable established a Task Force on Social Responsibility, both of which urged higher levels of corporate giving. One response to this was the establishment of two-percent "clubs" in various cities, movements on the part of businessmen to encourage increased corporate support of charitable endeavors. In addition, regional "grantmakers" groups, which acted as information and service mechanisms, opened their doors to corporate members.

This change in the climate for corporate giving was undoubtedly responsible for some of the increment in corporate contributions between 1979 and 1986. While a doubling of contributions amounts and percentages was a notable achievement, it was also a disappointment to those whose expectations were for an even larger growth in corporate giving.

Once again, it's not "philanthropy."

Prior to 1981 when the Congress raised the allowable deduction from 5 to 10 percent of taxable income, it was common to hear something like the following: corporate giving — which then was slightly more than $2.0 billion — amounts to only 1 percent of corporate profits before taxes; the tax law, however, allows corporations to give up to 5 percent; therefore, corporate contributions could be five times as much if the business community were only to do its duty by giving what the tax law allows.

That this was spurious reasoning and that these expectations were grossly unrealistic is obvious. But it does illustrate the awakening of interest on the part of many who had previously had only a dim awareness of corporate contributions. The error of reasoning was compounded in many instances by a tendency to equate corporate giving with foundation grants, an understandable confusion in light of the fact that many major corporations had their own sponsored foundations. Hence, the expression "corporate philanthropy" arose and became used frequently as a descriptive phrase for corporate contributions and some other aspects of corporate social responsibility.

But corporations, unlike foundations, do not exist for philanthropic purposes. Business corporations are entities whose purpose in life is far removed from charity. And we are talking about contributions of money and property that belong not to the corporations themselves but to their stockholders who are the legal owners. Corporations do have the power to make charitable contributions and they are encouraged to do so in a variety of ways, but charitable giving is, at best, an incidental activity in the corporate world.

The motivation for charitable giving is rooted not in altruism but in the corporation's own self interest. In the enlightened view of corporate management, there is explicit recognition that some sacrifice of short-term profits might be necessary if the ultimate self interest of the corporation is adequately to be served. As one observer put it:

> "Corporate activity in the social sphere is not, in fact, altruistic. It does not represent a purely voluntary and gratuitous act of generosity. It does not reflect a partial transmutation of the corporation into an instrument of social progress. It reflects a tactical judgment as to the most advantageous manner for the corporation to conduct its business in the light of the climate of opinion in which it must function. Nor is justification of the validity of corporate action in terms of its being "good business" outmoded. On the contrary, this is the fundamental test of whether the action -- even though involving gratuitous expenditures -- is intended to fulfill the objectives of the business."10/

That corporations do make contributions and gifts is simply a reflection of the fact that corporate management now recognizes that the long-run welfare of business depends, among other things, on the health of the society of which they are a part.

No two corporations are exactly alike. That being the case, each corporation determines how much to give, and to to whom and for what purposes, according to its own interests. In making that determination, corporate managers necessarily give weight to a host of factors, some of which are internal to the corporation while others reflect that external "climate of opinion."

As to a corporation's contributions budget, the most important single factor is the company's ability to give as measured by its earnings. A company with large profits will tend to give more than a company with small profits, and any one company's giving will tend to rise and fall as its profits increase and decrease. For all companies at a given profits level, however, there may be a wide range of giving levels; this reflects, among other things, differences in viewpoint among corporate managers as to what is appropriate for their respective companies.

There has been a trend, in recent years, for management to increase modestly the size of their contributions budgets relative to corporate earnings. For the most part, this reflects a reaction to the external factors that impinge on corporate giving.

Among these, as we have seen, are various changes in the tax laws and certain pressures arising from social and political change. All such factors have limited force and limited tenure, but while they are in place and effective they are instrumental in bringing about increases in the average amounts of giving per company.

Taken in conjunction with the dynamic growth of the corporate population and the probable growth of corporate profitability, it is an odds-on bet that total corporate contributions will continue to grow in the future. The question is: will it continue to grow as fast in the future as it has in the past?

Speculation.

Ultimately, of course, the rapid growth of corporate contributions that has characterized the last half century must come to an end, unless economic growth and corporate profits growth should increase to parity with it. Otherwise, corporate contributions as a percentage of corporate profits will rise without limit. In the long run, the growth of corporate giving cannot outpace the growth of corporate earnings.

Having said that, it is by no means certain that the the slowdown will occur in the next 12 or 13 years, or in the next 50 years for that matter. What actually happens between now and the year 2000 will depend on many factors whose future courses are highly uncertain. The following list is meant to be suggestive, not exhaustive:

(1) The health of the nation's economy, including the rate of economic growth and the growth of corporate profits before taxes.

(2) The stability of general price levels.

(3) Government policies, especially tax policy and the nature of the federal involvement in the social arena.

(4) The views of political leadership with respect to the balance between public and private initiatives in the social sphere.

(5) The general "climate of opinion" toward corporate contributions in society at large.

(6) The growth of alternative sources of funding for the nation's charities.

(7) The effectiveness and accountability of charities and the skill and sophistication of their fund raisers.

(8) The attitudes of corporate management with respect to the appropriate levels of corporate giving.

(9) The willingness of corporate stockholders to allow corporate contributions at any specific levels.

(10) The relative attractiveness of alternative means of response to the dictum of "social responsibility."

Clearly the ability and willingness of corporations to raise the levels of their giving in the future are in large part a function of developments that are outside the control of corporations themselves. The perception of corporate self interest will not go away, nor will there likely be any diminution of corporate interest in being socially responsible good citizens. What corporations actually do in the next dozen or so years depends most of all on the kinds of stimuli they receive from the external world.

In the absence of continuous stimuli -- new incentives for increased levels of giving and new forces leading to larger perceptions of corporate duty -- the rate of growth of corporate contributions is virtually certain to diminish.

The past growth of corporate contributions was certainly unplanned and much of it was the inadvertant result of actions that had quite different objectives (e.g. tax policy). The historical picture painted above reveals a series of influences that were almost accidental in origin, timing, and impact. Together they resulted in an extraordinary era of growth, one that is unlikely to be repeated in the future. Which is not to say that corporate giving will stagnate in the years to come. On the contrary, the corporate community has committed itself to underwriting its appropriate share of the nation's charitable endeavors and there every liklihood that it will continue to do so.

But corporations will continue primarily to be business organizations, and their charitable contributions will continue to be incidental to their principal purposes and objectives. Corporations are, after all, designed to produce and sell goods and services and to earn profits for their stockholders. To the extent that charitable giving is compatible with that design, one may expect it to grow as corporations themselves grow. At the same time, charity must be prepared to share the vicissitudes of corporate fortunes -- the business cycle, competitive inroads from abroad, industrial restructuring, and similar dynamic changes -- that affect the ability to give. The reality is that it's not philanthropy.

NOTES

1. This analysis is based on the perceptions of Courtney L. Brown, Dean Emeritus, Graduate School of Business, Columbia University. Dr. Brown has long been a participant in efforts to encourage corporations to increase their support of education and other charities. His observations were first articulated at a 1969 meeting for executives of a number of public accounting firms and published by the Council for Aid to Education.

2. Hutton v. West Cork Railway Company, 23 Ch. D. 654, 672 (C.A. 1883).

3. A.P. Smith Mfg. Co. v. Barlow, 13 N.J. 145, 98 A.2d 581, appeal dismissed, 346 U.S. 861 (1953).

4. _Voluntary Support of Education, 1985-86_, New York: Council for Aid to Education, 1987.

5. _Corporate Support of Education, 1986_, New York: Council for Aid to Education, 1988.

6. These data are from the IRS files of corporate income tax returns and are taken from a forthcoming CFAE publication, hereinafter referred to as "Update."

7. Thomas Vasquez, "Corporate Giving Measures," Research Papers Sponsored By The Commission of Private Philanthropy and Public Needs, Washington: U.S. Department of the Treasury, 1977, pp. 1839-1852.

8. Hayden W. Smith, _A Profile of Corporate Contributions_, New York: Council for (Financial) Aid to Education, 1983.

9. See Vasquez, Smith, and Update.

10. Phillip I. Blumberg, "Corporate Responsibility and the Social Crisis," _Boston University Law Review_, Vol. 50, No. 2, Spring 1970, p. 207.

SECTION THIRTEEN

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THE POLITICAL ECONOMY OF CHARITABLE GIVING BY ELITES IN THE UNITED STATES

by

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Prepared for the 1988 Spring Research Forum
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Public Policy and Philanthropy"

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This paper is based on additional analyses undertaken as a Visiting Fellow in the Anthropology Department, Princeton University.

THE POLITICAL ECONOMY OF CHARITABLE GIVING BY ELITES IN THE UNITED STATES

The philanthropic wealthy (1) and others believe that private contributions and nongovernmental organizations are integral to the American way of life. They contrast individual giving to charity with the taxation policies of European welfare states. Rich people want to be the ones who make decisions about where their surplus money goes, rather than having the government do so. They think their funding is better than the State's, and they believe services are provided most effectively and efficiently by voluntary agencies. This ideology is the basis of wealthy people's involvement in and control over charitable organizations.

There is a particularly strong tradition of individual giving and volunteering in the United States. The wealthy have always funded the arts and their favorite benevolent activities, as well as churches, hospitals, schools and universities. However, elites also derive greater benefits from nonprofit organizations than most other people. For example, they send their children to private schools and colleges that they help fund, or they enjoy cultural events, which they support philanthropically, to a much greater extent than those who cannot afford tickets. The poor and middle class have also been generous, especially to religious organizations, but they have had less to give. Individual donations, foundations, and other charitable devices provide the rich with authority, influence, power, and the reward of doing good.(2)

In this paper, I analyze philanthropic rhetoric,(3) especially as it relates to the political economy. The words of the wealthy led me to the conclusion that charitable giving and voluntary activities allow the rich to control nonprofits, provide them with many benefits, (4) and set them apart from the masses. Through their philanthropy the wealthy support upper-class institutions that reproduce the ruling class. And, in a related manner, other kinds of charity maintain a reciprocity between the upper and lower classes that may help to stifle rebellion or reform. Finally, and of greatest concern, philanthropy has recently served as a justification for minimizing the welfare role of government. The political economy of giving allows moneyed elites, rather than elected representatives, to exercise great leadership and control.

My interpretation is that philanthropy interacts with business and government, and cannot be fully understood without recourse to both. A fiction has been promulgated that three sectors of society -- business, government, and nonprofit enterprises -- operate independently. Yet, the freedom to amass and protect fortunes and to transmit them across generations is linked with tax policy and philanthropy. Recent income tax legislation has been increasingly less redistributive. Charitable and other provisions in estate law favor the accumulation of private wealth.

In addition, the government actually contracts out most of its services through either business or nonprofit organizations. For example, the roads that are funded by tax dollars are built by private firms. Medicare payments go to both nonprofit and for-profit hospitals. Social services provided by nonprofit organizations are financed almost equally by the government and private contributors. Economic, political, philanthropic, and social processes mutually determine one another.(5)

The rhetoric of giving is at odds with reality. Philanthropy is not an alternative to economic pursuits or politics, but a means of directing the way government spends its money. The rich do not necessarily get richer because of their philanthropy, but the poor rarely get richer or move up in economic status either.

Philanthropic Ideology

> If there were not a nonprofit community out there, two things would have happened. I do not think we would still be a democratic country. This may be exaggerated, but the public demand for the government to do this, that and the other would be to such a degree because of their needs... We would probably be a huge big government doing all these things, socialistic.(6)

Rich philanthropists equate their ability to make individual decisions about dispersing their wealth with capitalism and democracy. Their ideology is epitomized in their attitudes about charity, economics, and politics. Most rich philanthropists are opposed to the politics of the welfare state. Like other Americans, they are subject to a prevailing fear of socialism, which they incorrectly assume is the opposite of democracy. Or rather, as in the case of the millionaire just quoted, their view of democracy is closer to that practiced in the 19th century republics, wherein only the propertied class had the right to vote. They do not believe that the common people constitute the source of political authority. They hold that, while the masses may have the vote, the elected government should be limited in its power. The "public" cannot "demand" too much, whatever "their needs" might be.

A middle-aged Northeastern woman of wealth expressed her views: "We get closer and closer to an undemocratic society if we shift all the responsibility onto government. And that is what is going to happen if private philanthropy is discouraged." Once again, a peculiar idea about democracy is voiced, wherein it is undemocratic for the State to have major responsibility. There is little recognition here of the extent to which government contributions already fund nonprofit organizations in the United States,(7) but there is a notion that private charity can counteract or balance economic and state power.

This rich woman continued: "Somebody has got to take over or we are all going to be ciphers in some government sponsored social agency. I think it would be disastrous." She has an unabashed view about where control should rest. "Somebody," presumably an individual philanthropist and not the government, should seize power.

A set of beliefs like those of philanthropists is feasible because of an even more widely-held ideology that bolsters an artificial separation between the economy and politics, or business and government. According the Robert B. Reich, "American political rhetoric often frames the decision in the dramatic terms of myth: Either we leave the market free, or the government controls it."(8) One flawed myth holds that pure capitalism operates as if under natural law, that any interference with laissez-faire processes will lead to an economy in shambles. Government intervention and welfare provision must, therefore, be severely limited.

Rich people of every political persuasion made remarks about the importance of private nonprofit endeavors. Informants proudly referred to the history of charitable giving in this country, as well as their desire to fund projects that perpetuate traditional "American" values. Several different interpretations of what actually constitutes that tradition emerged, although an ethic of individualism and ethnocentrism pervaded many people's comments.

When referring to his family and company giving, a conservative Western grantmaker stated:

> We are defenders of the American Way. We believe that it is in danger. So organizations that address themselves to the preservation of the traditional rights, the traditional freedoms, and particularly the traditional responsiblity of the great American citizen we favor.

His interests are "primarily in education. I support things like the boys' club... and universities that appeal to me." He went to college at an Ivy League institution.

A liberal Easterner said that she thinks people give:

> [B]ecause of a very strong Judeo-Christian, American principle. I think de Tocqueville observed it, and it is true. We do believe, as American people, that we can change life for other people and for ourselves, and make it better. We really do believe that. Other societies, I don't think, have that belief.

She says she funds, "high risk, interesting ventures." These include the ballet, education and religious organizations. From her descriptions of these projects, only the private schools she supports are any kind of risk. They seem to be on financially shaky ground, in part, she implies, because they are ethnically and racially integrated, and provide scholarships for poor students. This liberal philanthropist might appear at odds with the conservative quoted before her, but their basic philosophies are close. Apparently, they both think it is up to the individual philathropist to determine what makes life "better."

Another example sharply highlights inconsistencies between political views, perspectives on charity and practice. A young funder who inherited his money and described himself as a leftist stated:

> I think the philanthropic tradition in the United States is very important. It is different from Europe... Europe does not give tax deductions for charitable giving... Individuals are not encouraged to give money there. So when they do, they give less... [T]he needy organizations fall under the government and the attendant bureaucracies. I think those societies move more slowly and individual initiative is not rewarded as fully. There is a rigid structure, that has to do with this interweaving of politics, bureaucracy, and the existing order.

He has been involved with other young rich people in an alternative foundation that has made grants to small local groups such as the La Raza Legal Center and the Medical Coalition for the Rights of Women. In spite of this young man's avowed politics, his outlook is totally consistent with philanthropic ideology, including what amounts to a kind of bald nationalism. Rich people who give to charity may not consciously understand the way in which philanthropy supports the larger political economy. They may even be critical of aspects of the system, but at the same time they are ardent supporters of the so-called nonprofit sector in the United States.

Rich people do not all publicly endorse the ideology just described, although most accept parts of it. A distinct minority of wealthy young activists, especially women, are giving grants for projects of social change. They may not like the current economic or political system, but they use it to promote their own ideas. A feminist funder dissented radically from even her progressive peers. She was the only rich person to say: "I am against the profit motive."

This woman views the world as a global political economy. Unlike most philanthropists, in addition to donating money to causes at home, she funds international, especially third-world projects. She gives away about $800,000 each year. On this she commented:

> I know it is a lot, but there are people with a whole heck of a lot more money than I have... [Where I come from,] we had a big house, but there were an awful lot of other people who did too. The money is there. It's an unusual situation on the face of the earth, where there is such a widespread group of people with money, even though it is small compared to worldwide poverty.

Along with a small number of grantmakers, she questions the business or governmental system. But in the final analysis, because of her contributions, she holds power over the projects she chooses to fund or not to fund.

An implicit social Darwinism is conveyed by many in the culture of philanthropy,(9) at both the personal and the group level. The general idea of this variant of social Darwinism is that elites are rich because they have greater skills and abilities than others, and therefore they are also better qualified to make decisions for other people. A self-made Texan commented: "If you have got enough sense to make the money, you ought to have enough sense to give some direction as to what you are going to do with it."

Business and Charity

The source of private donations to nonprofit organizations is business and investment income and profit. In this regard, there is an obvious connection between economics and philanthropy. The justification for the private provision of services is usually couched in economic terms. Most of the charitably minded wealthy believe that a freemarket system fosters a giving environment. An Atlanta philanthropist claimed that giving is strong in the U.S. today, because, "There is more money around." And, he continued:

> It is a matter of leadership. There is a pattern in the community that you can follow. ---- gave $50,000. She is worth $50 million. Somebody else worth a million dollars contributes $5,000... ---- makes six gifts of a million dollars each. [She's] worth 50 to 100 million.

Business people donate personal money to charity, which they often view as related to their work. Many companies, both small and large, are family controlled, and family members use profits for philanthropy. In addition, corporate giving or company-sponsored foundations award grants with funds donated by parent corporations. Business executives generally serve on corporate grantmaking committees.

It is difficult to separate business and personal interests, for they often overlap. A Midwestern businessman explained that philanthropy was vital in his community because: "We have a relatively small number of very wonderful families on the one hand, and the leadership of the business community on the other hand." In his town, the leading families own the leading companies. The mix of corporate and individual wealth varies by location, but all rich people have business interests. Historically and presently, business leaders are philanthropic leaders.(10)

Companies and the wealthy are unlikely to fund projects that might jeapardize their profits. One millionaire explained the corporate giving process. He said:

> It is a club. What is the phone company giving? What is the bank giving? What is the other bank giving? And everybody else falls into line, in proportion.

He also admitted, "We pretty much give to the same things, the safe things." It is not just that only the safe projects are funded, but that corporations systematically keep certain organizations from getting funds. He continued:

> If one guy [head of a company] has a problem with a neighborhood group, more than likely other corporations will have problems with the same neighborhood group -- like neighborhood groups that go after banks for not making loans... Well, suddenly, everybody's badmouthing this neighborhood group. I would guess they have never taken the time to personally visit the people about their concerns.

This situation may not be a cause of concern to most business people of America.

The predominant opinion across the country is that business comes before charity. In a temporal sense, this is obviously true, but once the money is made, it can used in any number of ways: reinvested to generate more income and profit, spent on consumer items or philanthropy. A California entrepreneur stated:

> The prevalent view is that a corporation's job is to make the shareholders' net worth grow. Then it is the shareholders function to decide what they want to do with their money. In this company we take a very narrow view of what our philanthropic obligation is. If it does not relate fairly directly to the interests of the company or to our employees, we pass it by.

Company giving programs reflect corporate interests, or the personal opinions of the chief executive, other officers, and owners. Corporate gifts may be clearcut contributions to charity or in the gray area of advertizing, public relations, or marketing.(11) The difference between corporate sponsorship of tax-deductible public television and commercial television is, for example, dubious.(12)

"Philanthropy is not a question of commitment, but one of economics," said one straightforward Eastern businessman. When asked about the process by which he makes his individual charitable decisions he claimed:

> It is what is good for the business. An example of that would be that somebody we are in business with is really strongly advocating their favorite charity. Or, we do it because of the connection of the individual, or because the charity is so linked with some business activity we are doing. A good example of that would be the [a private] University, which is a large client of the firm. We do a lot of business with them, and therefore we give to the University.

Universities are good cases in point. They may undertake substantial building and maintenance projects that they contract out to for-profit firms. They use investment counsel, lawyers, and a range of other professional services. In fact, most big higher educational institutions are very similar to large businesses.

Other examples of business connections with philanthropy were offered by a rich Midwesterner. He stated:

> We support well-made, basic charities. A typical example would be United Way and things of that sort And, [we] engage in special projects of public benefit which bear a significant relationship to our business, with particular emphasis on projects designed to prevent or reduce socio-economic losses... We are primarily in the insurance business. We pay for losses that people suffer, so we are very heavy into such things as traffic safety, worker safety, things that get into efforts to control arson, crime...

Much funding that relates to business interests is expressed as "for the good of the community," and often that community is the business community.

Millionaire philanthropists actively engaged in business tended to be the most candid about the charitable exchange system.(13) A wealthy Chicagoan advocates returns for philanthropic gifts.

> If you are giving you can ask for certain things back... Charity is not that much different from business. When you are making the investment in whatever you are making it in, you can demand certain things back.

A Boston philanthropist provided a specific example.

> Over the years, because I have gotten involved with a lot of people by serving on this committee [of a nonprofit organization] and that committee and this comisssion [usually refers to a government post] and that commission, I have met a lot of people in the business world. So there have been personal relationships established. The kind of thing that I do not usually say for the record is that it takes a lot of energy.

This individual consciously cultivates business and governmental contacts on behalf of nonprofit organizations. "As a director of the bank I am dealing with people who are into money. The other directors are heads of big corporations in Boston. So, I find that they are very helpful." In this case, another bank director had just sent a $5000 check to his colleague's favorite charity. The payoff may be made in any number of forms, in the business, government, or nonprofit arenas.

A woman philanthropist, whose husband is a commercial real estate developer, spoke of the advantages and disadvantages of attending charitable functions for business reasons. She explained:

> There are some people that we do pay back... I could care less [about this particular event] and he [her husband] could either. We are going because five or six people in his office wanted to go, so he is doing it as an office morale thing... People will come up to him all night tomorrow night to make a deal here and cut a deal there. People will come up to me and ask to be introduced and so on.

While she says she does not enjoy these activities, this woman is clear about their other than strictly philanthropic value.

A well-known philanthropist claimed:

> There is only one excuse for American business and it is to serve society. Profit is our reward... When business does not do its job, then we get punished with adverse legislation, stringent regulations, pressure groups of all kinds... It is in business' and the nation's best interest to have as large a proportion of the demand for services, whether it be social, cultural, educational, medical or whatever, filled in the private sector.

Here is one of the clearest explanations of the business component of philanthropic ideology. If the business community takes the lead and funds "for the public good" then its other activities are less constrained. In this straighforword way, philanthropy serves capitalism, but does business "serve society?"

Politics

Whether right-wing, conservative, moderate, liberal or left-wing, many of the charitably wealthy are involved in politics. This activity is a tangible link between philanthropy and the political economy. One millionaire said: "I have always been on [philanthropic] boards, even in my political years." Some have held or run for public office. The Rockefellers, for example, are probably the wealthy family most famous for both their philanthropy and roles in government. Many rich people have been appointed to high posts, such as cabinet seats. Others serve in Congress, the Senate, and in state government.

The giving practices of most philanthropists are related to their political beliefs and involvement. Except for tax purposes, no distinction is usually made between these activities.(14) When asked about charity, a funder from the Mid-Atlantic region said: "I give money to conservative causes." Another rich person said: "My original fundraising and giving away money was really encouraged in the political arena. I was head of [a committee] for George McGovern's presidential candidacy."

In a few cases the primary commitment is recognized as political, rather than charitable. A young man admitted that his motives for charitable giving are "almost purely political." Another funder who lives in Washington, D.C. stated: "I decided that I wanted to have an impact politically, and that one of the things people in politics listen to is money." Most philanthropists are like the middle-aged Eastern woman with moderate politics who suggested: "You cannot get away from politics, agendas for people... I am a Republican, and I have always enjoyed public affairs. I pay a lot of attention."

A fairly representative philanthropist indicated: "I have always been politically active, if you define politically broadly, not just electoral politics." Most charitable elites are committed to promoting particular causes through their philanthropy. One individual said:

> If you have something that you believe in that ought to be done, and you believe it is not being adequately addressed by an existing agency, then you have a powerful incentive to try to do whatever you can. Sometimes there is no way except to put up the money. You can go so far...with a minimum amount of your own money, and try to enlist the help of other people, and convince them of the merit of your idea. But if you get right down to it in the final analysis, some things just take money.

Whether through their charity or in the political arena, wealthy people exercise more power because they have more money.

Political activity involves more than individual or small group efforts, candidacies, and funds. Ideas, policy formulation, and the organization of political agendas are increasingly apt to come out of nonprofit higher educational institutions and so-called independent institutes. These organizations usually take the stance of being impartial experts outside of government.

For a recent example, the Heritage Foundation, a right-wing nonprofit think tank, gained prominence in the early 1980s with the finacial support of conservative philanthropists. Less than a week after Ronald Reagan had been elected president, Heritage had released a book

(15) outlining their recommended policy programs, and was sending resumes to the White House transition team. The Foundation had been formed ten years earlier with the express purpose of serving conservative Congressmen in need of intellectual support for their positions.

The shift to the political right, expert marketing and public relations, as well as substantial contributions help explain the success of the Heritage Foundation and similar organizations. Historian James Smith, who has been studying public policy research institutions, documents their "techniques of advocacy."

> "We don't make any bones about packaging and marketing," says Burton Y. Pines, the Heritage Foundation's vice president for research. And Edwin J. Feulner, Jr., the president of Heritage, describes Washington think tanks in general as "second-hand dealers in ideas," contending that "it takes an institution to help popularize and propagandize an idea-- to market an idea." (16)

But, Heritage is only one case. Smith estimates that there are over 1,000 policy think tanks in the United States and Canada. They include the American Enterprise Institute, the Brookings Institution, the Hoover Institution, and the Rand Corporation. Each has been accused of leaning one way or another on the political spectrum.

Interdependent Provision

> In the first year our company put up $400,000 and the state put up $400,000. And then I put in $400,000 which I had agreed to personally, so there would be some flexible funds there. In the second year the company had no obligation to continue, but did put in $250,000 and the state put in $3.8 million. Now in the third year the company put in $50,000 and the state is putting in $4 million to continue the programs.

According to the rhetoric of philanthropic elites, private giving plays a special role where the State cannot, does not, or should not, depending on the ideological proclivity of the speaker. In fact, governmental, corporate, foundation, and personal spending is generally complementary, as the case above illustrates.

The millionaire was personally involved in the nonprofit poverty project to which he refers. He acted as a broker, using his political influence and money to interest state officials in the program. His business made an initial sizable grant, with matching funds from state government. As an individual, he also donated the same amount toward startup, bringing the total first year budget to at least $1.2 million. These identical contributions gave the appearance of equivalency, but during the nonprofit program's formative period, the wealthy man had obviously invested more than the state when his company's money is also considered. He undoubtably had a good deal to say about what kind of project it was, how it would develop, and who it would serve.

In following years, presumably after the project had proved successful, the millionaire's company and personal contributions declined substantially, and the state was footing an increasing bill. While the nonprofit program was created by private initiative, its ongoing budget is funded by the government. The state is not running the project, but it is providing the bulk of the money. The wealthy man and other trustees continue to make policy decisions about agency operations, although there is state oversight. Ongoing funding is not guaranteed, but linked, rather, to political decisions. This particular poverty project will probably stay in good standing because of ties between its board and government officials.

These types of "public/private initiatives," as they are now called, are increasingly popular. The broker may be either a public or private entity or an individual. State officials with budget problems also try to sell their ideas to private investors. Joint projects may be undertaken in almost any type of venture, from the arts to welfare.

The way that social services are funded and provided is illustrative of problems endemic to the political economy of giving in the United States. In the area of basic human welfare, the government must be the major financier or many services cannot be delivered. Churches and other voluntary agencies may sponsor soup kitchens and shelters in particularly bad times, but they can never meet all the need. And, they do not solve the problems of, for example, unemployment, underemployment, and lack of adequate housing. Furthermore, the interviews indicate that it is not generally in the interests of the wealthy to fund social service programs. The millionaire just described is the exception, rather than the rule.(17)

That the government would have different priorities than private givers seems reasonable. Such priorities

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obviously shift, but for fifty years welfare provision has been considered a State responsibility. The introduction of the Social Security system after the Great Depression, and the later War on Poverty programs of the 1960s and 1970s, led Americans to expect that government would provide certain primary services. This expectation continues, but conservative priorities are not so different from those of the wealthy. With the Reagan Administration, a major policy change occurred and social services were hardest hit in the budget cuts.(18)

We have always had mixed political economy of giving in the United States, or what might be termed interdependent provision. In 1980, nonprofit organizations were providing more than half of the nation's social services, with funding from both the government and private sources. In the welfare field, slightly more federal tax revenue went to nonprofits than to government agencies.(19)

Recent changes in the shares contributed from private sources and by the State to these programs are clearest when viewed from the perspective of nonprofit budgets.(20) In 1977, the federal government was picking up more than half of the tab for private social service programs (53.5 percent). In 1984, however, conservative priorities had become well-established, and the State was contributing only 43.9 percent to the private part of the welfare bill. Curiously, the federal government was paying more in the area of nonprofit health, (35.3 percent, up from 32.4 in 1977); and less in private education and research, (17.0 percent, down from 19.1 in 1980).(21)

Today, federal, state, and local contributions to all nonprofit organizations are equal to total private giving, nearly 27 percent each. The remaining funds come from dues, fees, and interest income. However, only a third of all nonprofit organizations serve the poor, who are the least able to pay for services.(22)

If education, healthcare, and social welfare services were supported solely through tax dollars by the State, these services might be more equalized in terms of both quality and opportunity. A host of needs in all societies, and differences of opinion as to what makes for quality of life, create tensions about funding priorities. Since both education and poverty programs are important, how should decisions be made about their relative merits? Should any or part of these services be administered by voluntary agencies or the government, and at the local, state, or national level? And what about arts and culture? Should these remain the domain of the philanthropic wealthy?

Tax Policy

Charitable tax policy in the United States encourages private citizens to give to the causes of their choice, but does not provide for equity. Because they are able to make larger donations, wealthy people have disproportionate power within nonprofit organizations. Whether philanthropists have a particular interest in the arts or welfare, their voices, in many cases rather than those served, are the one's heard.

For example, according to the Internal Revenue Service, in 1984, the 16,295 individuals or couples with annual adjusted gross incomes of one million dollars or more claimed an average charitable contribution of $139,291 on their tax returns. The overall average deduction taken by all 57.5 million itemizers was based on $1,223 in gifts, slightly above the average $1,133 which taxpayers in the $30,000 to $50,000 bracket donated, and well over the $672 average claim of people who had made between $5,000 and $10,000 that year. In addition, nearly 23 million nonitemizers showed an average $51 charitable donation.(23)

Some hypothetical examples may clarify these figures. The anything but "average" millionaire who gave $140,000 to charity might have made ten gifts of $10,000 each to her favorite organizations -- or two gifts of $50,000 each -- and divided the remaining $40,000 among several nonprofits. A middle-class person probably wrote checks of $100 or less to ten or twelve causes. The $10,000 contribution, and almost certainly the $50,000 donation would put the wealthy person in a position of influence with from two to ten charities. The $100 contribution, which for most of us is sizable, would have gone into a pot of money over which the middle-class person has little control.

The real story is slightly more complicated. There is evidence that major philanthropists are the very wealthiest people in the country, those who Ferdinand Lundberg labeled the "super-rich."(24) A recent economic study on the charitable contributions of the wealthy, based on a stratified random sample of income tax returns filed between 1971 and 1975, found great variability in levels of giving, especially for those with the highest incomes. Researchers Gerald Auten and Gabriel Rudney suggest that "the reputation of the wealthy for generosity is largely the result of exceptional generosity on the part of a minority of high income givers rather than widespread generosity among the wealthy."(25) They also indicate that "the proportion of generous givers rises with income."(26) In the early 1970s, wealthier donors, who gave more to charity, made annual median contributions of about $435,000.(27) Let us assume, along with the economists, but discounting inflation, that this figure is more accurate than the average $140,000 that includes unestablished millionaires who are not very charitable.

The hypothetical multi-millionaire philanthropist has contributed $400,000 to the causes of his choice. He can dominate one organization, or he can have substantial leverage by donating $100,000 to four organizations. He may give $40,000 to ten groups, and still have a great deal of influence. He probably gave two or three large grants, and several smaller ones in the range of $10,000, which would offer him a significant voice in several organizations. In addition, he would contribute $1,000 to $5,000 to other organizations at the request of his friends and relatives. He is also raising money from them, and the government, for his favorite causes. And, he, his friends and relatives, and their companies and foundations are making contributions to each others' preferred charities.

Taxes do not have a direct affect on the amounts that the wealthy give to nonprofit organizations. But, as one typical philanthropist explained:

> The government makes it pretty attractive to you [to make charitable donations] in two ways: giving you a deduction for what you put into philanthropic purposes, and also taxing you at a very high rate if you do not.[1985]

Charitable tax incentives are of greater benefit to the wealthy than those in lower income tax brackets because the rich are able to substantially reduce the taxable portion of their income through their philanthropic contributions. The larger the gifts, the more they save in taxes and the greater influence they weild with nonprofit organizations. Furthermore, provisions in estate law allow the wealthy to set up charitable trusts that are virtually tax free. Interest income benefits nonprofit organizations the donor chooses and may even control, but eventually the corpus of the trust reverts to the donor's heirs.

In the last 30 years, top individual income tax rates have declined from 92 percent to 28 percent. The 1986 Tax Reform Act dramatically changed the top rate from 50 percent to 28 percent. This means there will be a greater direct economic cost to giving by individuals than in the past, but rich philanthropists will still recieve a deduction. The price of giving is 72 cents for every dollar donated to charity. In other words, when a wealthy person makes a $10,000 gift, it is really only costing $7,200, because of savings in taxes. It also means lost revenue to the government, but probably increased funds to nonprofits.

The comments of a millionaire help clarify the consequences of this policy. "I am sure I give away more because it is deductible than if it was not because I am sharing it with Uncle Sam. Instead of a Congressman telling me where my dollars are going to go, I am telling them where their dollars can go." He understands that money given to charity is an alternative form of taxation over which individual donors, rather than the legislature or civil service, make decisions. Add to this the statement of another wealthy philanthropist, "There is a feeling of power that goes along with all this, and a feeling of being able to hand it out."

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Notes

1 This paper is based on confidential in-depth interviews with 136 millionaires from across the United States. The interviews were conducted under my direction by a team of collaborative researchers as part of a joint Yale University, Program on Non-Profit Organizations/ Council on Foundations study (Odendahl 1987). Our goal was to understand the charitable motives and attitudes of the wealthy.

Informants were active in local and national networks of philanthropists. We spoke directly with 82 men and 54 women of wealth. The vast majority are both currently married and have children. This elite group is mostly white and Protestant, although 34 of the 98 participants who reported their religion are Jewish. About a quarter of the people interviewed are younger than 40 years of age. An equal number are either middle-aged or over 60 years old. Fewer than 10 of the informants are not college graduates. More than half of those for whom data are available graduated from Ivy League universities.

Manufacturing was the major original source of wealth for most of the philanthropists, followed by mining and drilling, the computer and high technology industries, real estate, and transportation or communication. A third of the wealthy people (43) are self-made, first generation millionaires. The rest inherited at least some of their money, or married into a rich family. There are 45 second generation heirs, and declining numbers in subsequent generations, with ten who are in at least the fourth generation from the original fortune.

2 Space limitations do no permit a full examination of these issues. In this brief introduction I am only able to outline my concerns about the consequences of elite control of nonprofits.

3 Wealthy individuals told me and the other interviewers what they wanted us to hear. On the whole, I assume that they believe what they said, and that their actions are based on their beliefs. With only a few exceptions, and outside my experience as Executive Director of the Women's Foundation of Colorado, my interaction with rich philanthropists and the information presented here was limited to the interviews. After a typically formal meeting concluded, I did not see those interviewed again, or engage in social or unguarded conversation. While I might have heard or read about them later, I never directly observed their behavior. Therefore, my evaluation of the effects of giving by elites is based on the relatively sparse, uneven documentation of where charitable money goes and how it is used, as well as what can be inferred from both the interviews and published data.

4 Due to a lack of statistical information concerning how much money goes to what organizations, from whom, and in what way those funds are used, there is no way to "prove" that elites tangibly benefit more than others, but the evidence points in that direction.

5 I examine the economic activity of government only in relation to philanthropy. And, my appraisal of the political activities of the wealthy is somewhat limited by the interview data. When we were conducting the research, we were not looking for these links, but they appeared as people spoke about their business and political interests.

6 This and all following quotations, unless otherwise indicated, are drawn directly from interview transcripts. See note 1 for details of the study.

7 Salamon, 1987, provides excellent documentation on government provision of services through nonprofit organizations. "Federal support to the nonprofit sector alone amounted to $40.3 billion in 1980. This represented about 36 percent of total federal spending in ... fields [served by nonprofit organizations]. State and local government own-

source revenues would likely add another $8-10 billion to this total... In addition to the direct government support... nonprofits also receive indirect support in the form of the tax deductions provided to their contributors. These deductions represent revenue that would otherwise go to the U.S. Treasury... According to the U.S. Office of Management and Budget estimates, these "tax expenditures" provided an additional $8.4 billion in support of voluntary organizations in 1980."

8 Reich, 1987, 222. The beginning of the "Epilogue" summarizes Reich's basic interpretation. "Political culture in America--as it always has been and will be, as it is anywhere else--is permeated by myth. Mythology is an indispensable conceptual shorthand, the means by which we comprehend, come to terms with, and talk about complicated social realities... America's political mythology can be rendered, with only slight gaps, exaggerations, and overlaps, as a set of four core parables: the Mob at the Gates, the Triumphant Individual, the Benevolent Community, and the Rot at the Top. The basic outlines of this mythology are enduring and uniquely characteristic of our culture", 235. Variations of these parables are found in philanthropic ideology. For the wealthy, "the mob at the gates" is the common people; "the triumphant individuals" are themselves; they fund "the benevolent community"; and the government represents a "rot at the top."

9 See Hall, in progress(a) for a historical explanation and analysis of the influence of Andrew Carnegie on present-day philanthropic ideology. Reich, 1987 also touches on this idea in his discussion of the recent rise of conservatisim, that "refashions resonant new versions of America's core myths." Reich explains that the latest "parable presents an intricate blend of dissenting Protestant theology and social Darwinism" (21-22).

10 See Hall, in press(b) for a historical treament of corporate philanthropy.

11 See Knauft, 1986, as well as White and Bartolomeo, 1982.

12 The only real difference is the markets that the public and commercial networks reach. When the Mobil and Exxon Oil companies advertize on public T.V., they are trying to reach elite opinion makers.

13 I am developing the concept of a charitable exchange system more fully in other work in progress. The basic idea is that none of philanthropy is truly altruistic, but that the giver always receives something in return.

14 By law, certain nonprofit organizations are limited in the amount of political advocacy they can undertake. Some groups get around these regulations by calling what might otherwise be considered lobbying, educational activities. A donor gets a charitable deduction only if the agency maintains its tax status.

15 Mandate for Leadership: Policy Management in a Conservative Administrations, 1980.

16 I am grateful to James Smith, who has shared early drafts of his manuscript in progress with me. "Introduction," page 24. See his paper in this volume, as well.

17 But he is typical in that he wants to have control in the organizations he chooses to fund.

18 See Hodgkinson and Weitzman, 1986, as well as Salamon, Musselwhite, and De Vita, 1986,3-38, for more details on the welfare cuts. It is important to note that, in contrast, there were minor cuts on the so-called "defense-side" of the national budget.

19 Salamon, 1987, estimated that in 1980, total federal spending in the social services was $7.7 billion. Of that, $4 billion went to nonprofit organizations, or 52 percent of federal support in that area. "In other words, nonprofits deliver a larger share of publicly funded services in these fields than do government agencies."

20 Because both taxes and private money pay for portions of social service programs, it is exceedingly difficult to accurately measure the total welfare bill in the United States. Salamon, 1987, explains that, "[N]o government-wide overview of Federal support to nonprofit institutions is available... [F]ew of these individual programs maintain data systems that make is possible to identify the scale of program resources flowing to nonprofit institutions. Similarly, few state or local governments collect data on this facet of program operations either. As a consequence, to examine government support to the vountary sector it is necessary to stitch together data from a a variety of disparate sources."

21 Hodgkinson and Weitzman, 1986, 7. Furthermore, Erie, Rein and Wiget, 1983, estimate that fewer than 3 percent of the nation's human service employees work for the federal government.

22 Salamon, Musselwhite, and De Vita, 1986.

23 AAFRC Trust for Philanthropy, 1987. Data for 1985 are incomplete, but the average contribution for itemizers in all income groups was $1,326, about $100 higher than the year before. Nonitemizer donations soared to a $373 average, as a result of increased understanding of the Charitable Contribution Law, which allowed them to deduct, above the line, 50 percent of their gifts to charity. The number of itemized returns in the $30,000 to $50,000 bracket had been declining, which probably accounts for increases in their average charitable donation.

24 Lundberg, 1968.

25 According to Auten and Rudney, 1987, 9, "the most generous 5 percent of givers account for 43 percent of total high income giving over the five year period and the most generous 10 percent account for 58 percent of total giving... For the $1 million and over income class, over 18 percent

contributed more than 20 percent of income, accounting for nearly 60 percent of the giving of that group," 31.

26 Auten and Rudney, 1987, 31. Over 700,580 tax returns were part of the sample. High income tax payers were oversampled, and sample weights were used to obtain population totals. There were 7,655 returns reporting income over $1 million. But, of these only 948 had a "permanent income of this amount. Therefore it appears that quite a few taxpayers had income that increased to the $1 million level only temporarily," 5. This is a fascinating and largely uninterpreted finding. Does it mean that from 1971 to 1975 at least 6,700 millionaires "lost their shirts," or is this an artifact of the weighting methodology? In any event, the study supports the notion that a small group of multi-millionaires are actually those giving the most money to charity.

27 Auten and Rudney, 1987, 32.

WORKING DRAFT

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FOUNDATIONS AND THE SHAPING OF PUBLIC POLICY

by

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Public Policy and Philanthropy"

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American political institutions seem to be afflicted by extraordinary grid-lock. They have been unable to act consistently on budget policy and are at loggerheads in fundamental areas of foreign affairs and defense. To observe the halting, faltering mechanisms from which our current policies emerge is to wonder whether the term "policymaking process" is an oxymoron.

Even in the best of times it is difficult to discern the who, what, and why in trying to explain how specific policies have taken shape, whether in the White House, in executive departments, or on Capitol Hill. It is more difficult still, as this paper will attempt, to move outside government in order to comprehend the part played in American political and decisionmaking processes by the many private, nonprofit organizations--foundations, think tanks, and advocacy groups--that operate on the peripheries of our formal institutional structures.

Twenty years ago at a time of much greater political confidence, Charles Lindblom described policymaking as "an extremely complex analytical and political process to which there is no beginning or end, and the boundaries of which are most uncertain." He saw policymaking as a "network of causes" and the play of power as, among other things, "a process of cooperation among specialists."(1)

The last years of the Great Society and the long decade of involvement in Vietnam have cast doubt upon what the specialists knew, upon their claims of neutral expertise, as well as their capacity for cooperation. The decade of the 1960s began with a celebration of the "politics of knowledge" and the "end of ideology." The late 1960s saw an abrupt end of the end of ideology, and the 1970s witnessed the arrival of a self-consciously ideological politics. Arguments about "conservative" and "liberal" philanthropy broke out; questions about political advocacy and the political effectiveness of grantmaking were asked as if foundations had been at the very core of public policymaking and policy outcomes. Had conservative foundations and think tanks brought about the "Reagan revolution?" Were their liberal counterparts responsible for the fifty year liberal ascendancy? Would they be in a position to defend the American welfare state?

Lindblom's insights remain helpful in trying to understand the place of foundations in American public policymaking. They temper any vain assumptions about the influence of a single actor or agency in public policymaking. And despite the discrediting of specialists and the populist suspicions of expertise that are never far beneath the surface in this country, Lindblom reminds us that policymaking has increasingly become a matter for experts and professionals. Experts are central to the "network of causes" shaping our public policy. To examine the role of foundations in policymaking is to see how the network of causes and the cooperation of specialists has evolved over the course of this century.

Today, foundations and their offspring--research centers, advocacy organizations, ad hoc task forces and commissions--are rarely among the proximate influences able to account for a particular legislative enactment or executive decision. Elected and appointed officials and their sizeable staffs obviously have much more to say about policy results than those outside government. It is possible on occasion to point to a specific commission report, the author of an influential study, a foundation-sponsored demonstration, or the scholars engaged in a long term research project and trace their impact on policies.

But the lines of influence are always difficult to connect. Kermit Gordon, president of the Brookings Institution during the late 1960s, an era when it was unrivalled among Washington policy research institutes, said in trying to explain Brookings' influence that "the path along which (research) affects decision making is so tortuous that the trail usually becomes difficult or impossible to follow." "In the end," he wrote, "the initiative may be decisive in inspiring an important policy decision, but it will have been strained through so many filters and combined with so many, other ingredients that the causal chain may be untraceable."(2) What is true of policy research is true of other foundation-supported endeavors. Where the play of ideas and influences is so intricate, generalizations about the causes of specific policies must be offered cautiously.

Policies have their own histories; they are narratives as individual and quirky as human biography. The accidents of historical timing, the tenor of personal relationships, misunderstandings, good fortune and diligent individual effort are among the keys to comprehending how particular policies are initiated, discussed and formulated, and then given shape within our formal institutional processes. As one moves back from a particular policy to seek its intellectual origins or to trace the contours of discussion before ideas become bills, laws, or executive orders, the analytic tasks are more problematic.(3)

In a political system as open to diverse outside influences as ours, the making of public policy begins at a great remove from legislative chambers and executive agencies. However, the dynamics of policy initiation have attracted considerably less scholarly attention than the formal political processes of enacting legislation, devising administrative regulations, and administering policies. Where do policy ideas originate? How do policy ideas with academic beginnings make their way from scholarly conferences, journals, and published studies into the formal policymaking process? How do ideas move from the inchoate, sometimes cacaphonous realms of thought, talk, petition or protest to be embodied in law, regulation, or executive order? This is the arena in which nonprofit institutions, especially foundations and research institutes, have tended to operate. (4) It requires that the scholar look less to policy outcomes and results than to the ways in which the network of policy causes has changed over the years.

In less than a century American philanthropic foundations have done much to shape and reshape the framework of policy causes. Their influence has been felt in at least four ways: 1). They have been of influence in financing or instigating a variety of institutions, both public and private, which have sought to bring applied knowledge to bear on public problems. 2). They have brought about changes in the professional training and intellectual perspectives of many of those who are either employed in government or engaged in research in universities and think tanks. 3). They have played an important part in creating the framework--books, journals, conferences, educational endavors--within which experts and citizens talk about public issues. 4). They have been more important than any other group of institutions in propagating views about the role of social science and organized intellectual inquiry in public affairs. While they are certainly not the exclusive cause of changes in these areas, they are of major significance. What changes have they wrought? A paper of this brief scope can touch only lightly upon a few incidents and examples.

Institutional changes since the early 1900s and the ways in which those changes have altered the framework of policymaking--and the role of nonprofit institutions in it--are exemplified in two legislative enactments separated by just over half a century: the Budget and Accounting Act of 1921 and the Congressional Budget and Impoundment Act of 1974. The Institute for Government Research (forerunner of the Brookings Institution) was established in 1916, with financial and organizational help from men clustered around the burgeoning Rockefeller philanthropic endeavors. IGR's instigators, most of whom had been interested in reforming local and state governments, were keen on bringing sounder managerial techniques to the federal government. Their most eagerly pursued goal was to reform Washington's chaotic budget-making and accounting procedures by urging the President and Congress to establish a coherent executive budget procedure. (5)

With a gestation period of nearly two decades the Budget and Accounting Act of 1921 owed its intellectual design and passage in the final stages to the work of IGR staff members. From drafting both the House and Senate bills and arranging the hearings to technical help in setting up the Bureau of the Budget, IGR played the leading role. No private group will ever be able to play such a role again. Expert congressional staff(virtually nonexistent in 1920, now totalling 3000 on congressional committees) and hundreds of competing private organizations will see to it.

Through the 1920s, IGR continued to work with executive branch agencies in setting up managerial systems that dealt with budgeting, personnel, record-keeping, and internal organization. Focusing on the Executive Branch and inspired by the traditions of scientific management and the new field of public administration which it did so much to shape, Brookings was concerned early on with administrative efficiency.(6)

If IGR's hand was clearly visible in creating the Bureau of the Budget in the 1920s, Brookings was present and prominent but its role less clear-cut in the efforts to reform the budget process in the 1970s. Since 1971(with about $1 million from the Carnegie Corporation and the Richard King Mellon Foundation and another $1 million from its own operating budget) Brookings had produced a series of volumes, Setting National Priorities, that examined the president's yearly budget proposals. The Brookings analyses of competing budget choices and their long term consequences were sought out by congressmen and their staffs, government officials, journalists, and academics; circulation of the annual budget volumes peaked at more than 30,000 in the early 1970s. Through those studies and their earlier work on government finance, Brookings researchers earned a status as independent authorities on the budget and were called upon throughout the budget cycle to testify and give seminars.

But the legislative debates which preceded the passage of the 1974 budget reforms show how much more complex the legislative process had become. At the height of the budget battles between President Nixon and Congress there were over 250 bills and resolutions introduced to reform the budget process. While a Congressional Joint Study Committee offered the leading proposal, the process was compounded by proposals emanating from partisan study groups, individual members and their staffs, various subcommittees, and others outside of Congress. (7)

Brookings and its foundation sponsors influenced the budget reforms in many intangible ways and perhaps in one explicit way. They had demonstrated with the Setting National Priorities volumes that congressional budget making would be well served by a research staff to support its work(although, ironically, when it came time to testify on plans for a Congressional Budget Office, Alice Rivlin, who would later head CBO, testified against it, wrongly, as she now concedes). The staffs of CBO and the new budget committees would soon total about 350 employees. The procedural changes and the professional staffs working for Congress altered the network of causes shaping budget policy. Under Alice Rivlin, CBO's early annual reports were patterned on the Setting National Priorities volumes; they quickly surpassed the Brookings' volumes thanks to more timely data and greater analytic resources at the command of a government agency. Brookings' very successful publication series became less important to policymakers and its circulation began a steady decline(its use by the late 1970s was limited mainly to the college classroom).(8)

The creation of Brookings, the Budget Bureau, and Congressional Budget Office are indicative of how the institutional framework of American policymaking can change, altering the role and influence of private institutions. Brookings was virtually alone among research institutions in Washington in 1920; today there are approximately 100 private research centers and institutes in the capital and over 1000 across the country concerned with policy issues. (9) Although it is hard to draw a sharp line between research and advocacy groups(many of which also contribute research to public debates), the latter have become even more numerous. The number of government agencies doing research and analysis has also increased; OMB identified no fewer than 36 executive branch offices engaged in policy analysis in the early 1970s.(10) The staff of the Congressional Research Service, to take but one example, is roughly ten times larger than the staffs of Washington's largest think tanks.

Foundations and the private research endeavors they have spawned have exerted a consistent pressure to make the federal government more expert in what it does. The building of those institutions has gone hand in hand with the training of the researchers and analysts who populate them. Arguably, the greatest long term contribution foundations have made to public policymaking has been in supporting the infrastructure of American higher education. It is no coincidence that the American philanthropic foundation appeared at the turn of the century just when the now familiar social science disciplines began to emerge from the older study of history and political theory. Foundations, especially the Laura Spelman Rockefeller Memorial in the 1920s, built both the disciplinary infrastructure of the social sciences within the leading graduate universities and supported applied research projects. (11)

Two projects separated by four decades are exemplary. The research on business cycles initiated by Wesley Mitchell and his colleagues at the National Bureau of Economic Research in the 1920s(with timely support from the Commonwealth Fund and the Carnegie Corporation) was conceived as a huge data-gathering effort. Mitchell and his colleagus were nothing if not patient to see results. It was a project beyond the capacity of individual university economics departments(where graduate students were too few and the commitment to research indifferent) and it was not yet something that a government department was willing or competent to do. While Mitchell exercised characteristic restraint in making any claim that the growing understanding of business cycles had immediate policy uses, the work of N.B.E.R. would usher in significant change. With the help of N.B.E.R. staff members, the initial work on economic indicators was taken over by the Department of Commerce in the late 1920s. Many of the statistical indicators of economic change that are issued by federal agencies have their origins in N.B.E.R.'s work. (12)

The consequences for federal economic policymaking have been profound. The arrival of the social sciences, especially economics, as a tool for government administration and management is symbolized by the Employment Act of 1946. In creating the Council of Economic Advisers, the act gave formal policy advisory status to professional economists; in avowing a federal responsibility for the nation's economic well-being across the business cycle, the act also helped to institutionalize macroeconomic analysis. While the intellectual consensus upon which macroeconomic policy rested owed much to Keynes and his American interpreters(as well as widespread fears of a post-war depression), many of the tools which were used in policymaking had been designed and crafted in the "economics laboratory" of N.B.E.R. Long-term foundation support for the discipline itself was instrumental in making economics the preeminent policy science in post-war America, with all the consequences that that discipline has for the way we think about public policy.

During the 1970s and 1980s deregulation has been one of the consistent policy goals of both Democratic and Republican administrations. The ideological battles of the 1980s, however, have tended to obscure the origins of the movement to dismantle parts of the framework of economic regulation that have evolved since the 1880s. (13) The self-consciously conservative philanthropy that has spurred the growth of conservative think tanks and that has endowed university chairs and research centers in the name of free enterprise has played a part. So, too, has corporate giving for policy research and the greater corporate involvement in public policymaking through political action committees and corporate public affairs departments.

The broad popular consensus that brought about deregulation in the 1970s had already begun to take shape within the economics profession during the 1960s. Deregulation could not have proceeded without it. A Ford Foundation grant to the Brookings Institution in 1967 is exemplary of the ways in which changes within a field of study precede the coalescence of academic research and political opinion into policy. In the mid-1960s staff members at both Ford and Brookings lamented the dearth of economists(and other social scientists) interested in microeconomic questions and especially in studies of productivity in regulated industries. With grants eventually totalling $1.8 million Ford supported a Brookings project on government regulation.

The project proved administratively cumbersome but managed to involve junior faculty and graduate students in research projects and workshops at some of the nation's leading universities. While Brookings produced thirteen books(and a considerable number of articles) on the regulation of energy, transportation, communications and other industries, the major consequence of the research program was to direct many young economists toward questions of regulation and into the analysis of specific industries. If "policy is people," as some in Washington suggest, the redeployment of economists into the field of regulation was a necessary first step for the policies that followed in the 1970s. It was less dramatic and less visible than the conferences, seminars, and media-oriented projects emanating from the American Enterprise Institute, but it was a necessary prior step for the policies that followed.

Foundations have also played a central part in shaping the framework for public discussion and the quality of our public discourse. It is an amorphous subject and scholars have paid too little attention to it. From their beginnings in the Progressive Era, the oldest policy research institutions saw their mission as one of improving discussion of public issues among both professional researchers and the citizenry. In 1906 when Margaret Olivia Sage, widow of the wealthy and ruthless railroad investor Russell Sage, was searching for a way to use her late husband's wealth for some beneficent social purpose, her advisers solicited suggestions from many prominent people about how best to use the money. The consensus was striking. Virtually all agreed that there were too few journals and books, no major libraries or research collections on social and economic issues, and too few opportunities for communication among social researchers and activists. A program of research and publication was a novel and useful idea in the early 1900s. The Russell Sage Foundation, the prototypical think tank, devoted its resources to those tasks. (15)

At the turn of the century only some 6000 books, fiction and nonfiction taken together, were published each year. Academic journals had only recently been started by the scholars who, beginning in the 1880s, banded together discipline by discipline to form professional associations; a handful of university departments sponsored regular journals and publications series. A few reform associations and settlement houses issued publications; "muckraking" journalism gave a certain vitality to popular magazines. The basic infrastructure for communicating research findings and fostering public discussion was in the rudimentary stages of development. Specialization had not yet fragmented disciplines or rendered research completely unintelligible to the layman.

The framework for both professional and popular communication on matters of public consequence has changed dramatically. The development has been driven by commercial and technological factors as well as by the professional academic imperatives to publish and survive. Today roughly ten times more books are published each year than were issued at the turn of the century; over three hundred journals are listed in the Social Sciences Index, without beginning to exhaust the numbers of journals that treat public policy issues. In the mid-1980s my own survey of twenty-five of the most prominent public policy research oganizations in the United States has tried to assess their contribution to the flow of printed matter. In these years they have annually issued approximately 250 books and over 1000 reports, conference proceedings, lecture series, and papers, not to mention countless op-ed pieces and newspaper articles(some of the larger think tanks distribute over 200 op-ed pieces per year). Many think tanks now publish journals as well, ranging from the scholarly Brookings Papers on Economic Activity to the more lively and polemical Policy Review published by the Heritage Foundation.

There are no simple conclusions to be drawn in trying to evaluate the consequence of this flood of publications. It is easy to lament the fragmentation of knowledge and the inconsequentiality of greatly over-specialized research, but there is also much of value that emerges. It is worrisome to see the fissure that seems to have widened between what the experts have learned and what the citizen knows or believes. It does seem that those who met in Margaret Olivia Sage's Fifth Avenue mansion in 1906 and planned a program of research and publishing and the Russell Sage foundation staff members who over the next two decades worked in the Department of Surveys and Exhibits to make research findings accessible to a broad citizenry were well attuned to the public uses of social science research. Some think tanks and advocacy groups have proved very skillful over the past decade in using sophisticated public relations techniques to join the political debate as advocates of specific policies. They have reached out to a wider public. But this observer remains very concerned about the fractious and ideological tone of contemporary American political debate.

Questions about expertise and advocacy, science

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and ideology, cannot be addressed adequately in a paper of this brief scope. However, it is worth reflecting briefly upon the metaphors (and illusions) that have animated foundations and their beneficiaries as they sought to develop the social sciences, build research institutions, and try to apply research and expert knowledge to our social, economic, and political affairs.

When the oldest general purpose foundations began their work after the turn of the century they were driven by the optimistic conviction that they could create a science of society that would somehow deliver the nation from the divisiveness and corruption of politics. Science and philanthropy were public endeavors, but they seemed to promise a deliverance from politics.(16) The central scientific metaphor for those engaged in philanthropy and social science research in the early 1900s was drawn from the field of medicine. Whether it was Frederick T. Gates sermonizing about the importance of philanthropy to the Rockefellers or researchers from Russell Sage looking at urban tenements, they believed they could identify the root causes of social ills and that there were cures to the disorders of the social and economic system.

That scientific metaphor has been succeeded by others as social scientists looked to the quantifying physical sciences in the 1920s and to engineering and systems analysis in the 1950s and 1960s. There have been bouts of disillusionment as well. It is not clear, today, that even a tempered confidence in the social sciences will emerge anytime soon. If a new scientific metaphor can be glimpsed, a metaphor more appropriate to these cautious and fiscally-constrained times, perhaps it is the notion of social experimentation.

Beginning with the negative income tax experiments of the late 1960s, other experiments such as Rand's fifteen-year-long health insurance study, have proceeded rather unobtrusively through the 1970s and 1980s. Experimentation, grounded as it is in large scale medical and clinical trials, marks a return of sorts to the older medical metaphors. It is also a reminder of an enduring strain in American political thought--that the nation itself is an experiment. In recalling the various scientific impulses that have so often been embraced by American philanthropy, one hopes to recall a tradition that has looked skeptically upon short-term policy advocacy and critically upon simplistic notions of ideological philanthropy, whether it be liberal or conservative.

Notes

1). Lindblom, 1968.

2). Gordon, 1970.

3). "Public policy" is a term with various meanings. In the first pages of this essay I am using it in its most specific and narrow sense: an Act of Congress, an Executive Order, a government regulation. "Public policy" can refer to a cluster of decisions and programs that taken together embody government's aims and methods in approaching a particular area of responsibility. "Public policy" can also refer to a broadly stated goal or intention of an administration.

4). Two books that do consider the origins and sources of public policy innovation are: Polsby, 1984; Aaron, 1978.

5). An excellent account of the origins of Brookings and the scientific management movement out of which it sprang is: Critchlow, 1985.

6). On the budget acts and the evolution of two of government's expert agencies, OMB and GAO, see: Mosher, 1984.

7). On the budget process in the 1970s: Schick, 1976 and 1980; Ippolito, 1981.

8). Interviews at Brookings with Alice Rivlin and Charles Schultze helped my understanding of the *Setting National Priorities* series as did conversations with former Ford Foundation staff members, Marshall Robinson and Peter de Janosi.

9). I have compiled a list of just over 100 Washington-based policy research organizations while doing research for a forthcoming book on think tanks; scrutiny of the Gale Publishing Company's *Research Centers Directory*, 1984-85, provides the basis for my national estimate. Because definitions of "research center" and "public policy" are inevitably debatable, numbers are imprecise.

10). Cited in Meltsner, 1976.

11). Useful studies of the social sciences and American universities include: Geiger, 1986; Bulmer, 1981 and 1984; Sutton, 1987.

12). On N.B.E.R in the 1920s: Mitchell, 1937 and Alchon, 1985.

13). Some perspective on regulatory policy is offered by McCraw, 1984; Derthick and Quirk, 1985.

14). On conservative foundations and the involvement of corporations in politics during the 1970s: Blumenthal, 1986; Reeves, 1985; Edsall, 1984; Useem, 1983.

15). The early history of Russell Sage is recounted in: Glenn, Brandt, and Andrews, 1947.

16). On the emergence of the social sciences: Haskell, 1977 and 1984; Furner, 1975.

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CORPORATE PHILANTHROPY AND PUBLIC REPORTING: SUNSHINE OR SHADOW?

by

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INTRODUCTION

During the early 1980s corporate contributions increased substantially each year, and in 1983 surpassed foundation contributions for the first time ever. Equally significant has been the growth of corporate donations from the 1% of pretax profits that had been virtually a constant for several decades up to nearly 2%.[1]

However, as international competition has overtaken many American industries, as merger-mania has turned corporate board room tables upside down, and as American businesses are making wholesale staff other cuts to adjust, corporate philanthropy has slackened its pace. During the 1981 through 1985 the average annual growth rate was 13.5%. But in 1986 it was only 2.3%.[2] And according to the Conference Board, based on its most recent survey of 387 major corporations, 1987 will register a 2% loss.[3]

Nevertheless, corporate philanthropy, while currently undergoing great change, appears here to stay as an important part of the philanthropic landscape. United Ways depend on it for a quarter of their revenues (United Ways also obtain another 50% of their income from corporate employees through annual business charity campaigns). Educational institutions, as the largest recipient category of corporate philanthropy, depend on it. Arts organizations have found diverse ways to increase their dependence on it. Untold numbers of other local community institutions also depend on it. And, if Marvin Olasky is to be believed, public policy groups of the left depend on it far more than of the right.[4]

CORPORATE PHILANTHROPY: SHROUDED IN SECRECY

Yet today, for all its importance, corporate philanthropy is still basically shrouded in secrecy. Whether considering its finances, governance, giving priorities, application procedures, non-cash contributions or even the identity of its grantees -- corporate philanthropy is essentially a mystery.

Those receiving the corporate largesse obviously know the passwords to gain entrance to the corporate coffers. But the many who aren't now corporate grant recipients, but who want to be, are given few clues as to whom to approach, how, when, for what and for how much.

Lack of information also bedevils those seeking to understand more of the nexus between corporations and charities -- whether the Capital Research Center (Patterns of Corporate Philanthropy),[5] The Council on Economic Priorities (Rating America's Corporate Conscience),[6] the enterprising Los Angeles Times, the Wall Street Journal, the New York Times or other media.

THREE EVENTS SIGNIFYING LARGER TRENDS

Three recent events stand out as indicators that this status quo may not be allowed to continue, though in NCRP's experience change will not come quickly. Last June for the first time ever the media met the charity world in a civilized confrontation in the *Chicago Tribune* Tower, 25 to a side, arranged by Nick Goodban and the *Tribune* Foundation and Craig Smith, editor of the insightful *Corporate Philanthropy Report*. The goal was to understand each side better. The charities wanted better media coverage of their good works, of course. The media said it covered charity when there was news, and would not be used as a free P.R. agency. The searing expectations of each world were like passing trains in the night. Nevertheless, what emerged were clear indications that this event was not a meaningless effort in the wilderness, but instead an event signifying the trend of increasingly greater media interest in charities and vice versa.[7]

The second event was a meeting in a pleasant basement room of a Washington, D.C. hotel, arranged by the Council of Foundations, bringing together several gray eminences of the foundation world (Merrimon Cuninggim, Paul Ylvisaker, Homer Wadsworth, among others), salt and peppered with two women and one minority foundation world representatives, a few progressive and one rightwing grantseeeker/ public policy types. After 1½ days this group came to agreement that the promotion of private philanthropy, particularly foundation philanthropy, would be best accomplished in two ways: by having more independent, not necessarily academic, studies of the field, particularly of public and private policies that impact it, and by having more investigation and analysis of abuses in the field. Whether or not action will be taken to make these things happen remains to be seen. But regardless, that this mostly establishment group, with long recognized foundation leadership well represented, came to such a consensus about how best to improve the field is startling, considering how recently the foundation world preferred instead the ostrich approach to self-examination and public interaction.[8]

The third event took place on Capitol Hill, also in Washington, D.C. This was the passage at 1987's end of Congressman J. J. Pickle's bill inflicting new disclosure requirements and financial penalties on most charities (HR 2942). After two days of hearings in the Spring, Pickle rushed his subsequently written bill through the Ways and Means Committee and the House of Representatives, and prevailed in conference with a Senate Finance Committee which didn't agree on the necessity of the bill, but bought it anyway as part of the omnibus FY 1988 spending bill.

Pickle was mad at Carl (Spitz) Channell, his aid to the Contras in Nicaragua and his aid to Pickle's political opponents. But this anger spilled over to new law that will affect all 501c3 charities and other tax exempt organizations. Greater disclosure will now be required of public charities than of private foundations, in some respects. And a whole series of tax penalties were enacted to discourage violation of the new disclosure provisions. The details aren't important for this discussion. The important lesson of this event is the shocking rapidity with which this legislation proceeded, without any hearings on the bill itself along the way. And while some new law was written concerning what is and is not prohibited to 501c3 organizations, the essence of the Pickle bill is to require substantially more disclosure.[9]

These three events -- the media-charity confrontation, the foundation gray eminences' consensus on priority action to better the field, and the Pickle bill requiring charities to disclose more than they've ever had to -- suggest that the era of openness and disclosure, that dawned in the 1960s, grew substantially in the 1970s and has been reported near death in the Reagan 1980s, is indeed very much alive and well, and growing in strange new places.

Add to this the perception of Dave Johnston, Los Angeles Times, that there is "a growing national movement ... challenging foundations to be more open about their policies and finances."[10]

Corporate philanthropy's existence behind the veil of secrecy cannot continue indefinitely. Indeed the rightwing Capital Resea Center's 1987 study of corporate philanthropy and the progressive Council on Economic Priorities' 1986 study of the "corporate conscience" indicate fresh interest in this subject in which only grantseekers, and corporate contributions officials had previously showed interest.

THE CURRENT STATE OF CORPORATE PHILANTHROPY AND PUBLIC INFORMATION

What then is the state of public reporting by corporate philanthropy? What proportion of corporations are publishing anything about their contributions programs? Are any corporations doing superior jobs? How many? Who? What information is mostly provided? What least? What information should be provided? For grantseekers? For the public at large (media, interested public policy centers, legislators, public officials, private nonprofit leaders)?

In order to answer these questions, the National Committee for Responsive Philanthropy (NCRP) undertook a study of the 200 largest profit-making corporations (using Forbes magazine list in 1985). We examined the printed information that these corporations provided voluntarily and routinely to grantseekers and the general public. The study encompassed both corporate foundations and direct corporate giving programs.

This was not a study of corporate giving to public affairs organizations, as was Olasky's study, nor of the size and nature of corporate contributions, as was the Council on Economic Priorities' effort. We sought to make no judgements on the worthiness of grants or grantees.

Our simple goal was to ascertain the availability of information itself and the quality or usefulness of that information from the standpoint of grantee and the general public.

STUDY METHODOLOGY

The contributions officer in each of the 200 largest profitmaking companies was carefully identified, and, if the company had a foundation run separately from a direct giving program, both contributions officers were identified.

With advice from five corporate executives and a corporate consultant, a letter was prepared explaining the background and purpose of the study, and requesting all printed information on the corporate foundation and/or direct giving program. Up to three written requests were sent to each business, and up to three followup phone calls were made if necessary.

By summer 1986, all 203 corporations[11] had responded either in writing (172 responses) or verbally, even if to say they had no information to send. None said they had no contributions program.

As a control, a cooperating nonprofit organization made similar requests for information to most all the same corporations, seeking the information as if it were a grantseeker rather than a public interest group embarking on the study (such as NCRP projected itself). In the 12 cases where this other organization received more information than NCRP, these responses were incorporated into the study.

Meanwhile, criteria were developed to evaluate the quality of information made available. We started with the same criteria NCRP had used to evaluate foundations' responses to a similar study in 1980 (Foundations and Public Information: Sunshine or Shadow?).[12] Nineteen people working directly in corporate philanthropy and 14 non-corporate persons involved in overseeing corporate social responsibility were asked to identify items in the foundation study criteria which were inappropriate or unfair to expect from corporations and to suggest additional useful criteria. They were also asked to comment on the original scheme of differently weighting different types of information.

The final criteria and weighting scheme were selected by NCRP. They do not represent a consensus of those consulted, though it is fair to say that they incorporate suggestions from a wide range of corporate officials and critics.

The 27 final criteria encompass six different areas:

A. Information on kinds of grants possible (including overall purpose and funding policies);

B. Procedures for proposal application and evaluation;

C. Information on grants (a specific, recent listing);

D. Governance of corporate giving program;

E. Finances; and

F. Non-cash or in-kind contributions.

Each of the 27 criteria was given either a weight of 3 or 6, depending on its relative importance. For instance, if the material contained the "purpose of the corporate giving program," 3 points were scored. But if a "statement of program/funding interests/priorities" was provided, 6 points were given, since this was seen as more important information. Sometimes, information submitted was less than complete, in which case less than 3 or 6 points was scored. There was one exception to the basic 3/6 weighting scheme. Having a complete grants list for one or more years counted 12. A total score of 129 was theoretically possible on this "disclosure scale."

See Appendix A for the complete list of criteria and their weighting.

After all the materials had been gathered from each corporation, they were read and a rating form filled out. In order to make this process as objective as possible, two different staff people prepared a rating form for each corporation. When all materials had been reviewed, the two forms for each corporation were compared to make sure there were no discrepancies. When differences arose, the materials were re-examined and an attempt made to reconcile the differences. If the two staff people could not reach agreement, a third staff member was called in to arbitrate. There were few instances where it was difficult to resolve a difference. If a difference about a particular item persisted, the corporation always got the benefit of the doubt.

Once all the items had been rated for each corporation, each staff person then independently marked down the scores. The two sets of forms were then compared to make sure that the correct scores had been assigned for each particular item. Section scores and total scores were then calculated both manually and by computer. Results were compared and differences corrected by referring to the individual rating forms. The final scores were cross-checked and computerized by the Public Interest Computer Association.

FINDINGS: SUMMARY

- Roughly one-quarter (46) of the nation's 200 largest profit-making corporations make absolutely no contributions information available to grantseekers or the public -- even after repeated requests for such information.

- On NCRP's scale to measure the quality of disclosure, only one corporation scored higher than 75% of the maximum possible, and only 27 corporations (of the 203 studied) scored better than 50%. If better than 50% is considered a "high" score, then few (13%) of the country's major corporations meet high standards for disclosure.

- The median of the 203 businesses studied was 29, equivalent to 22% of the maximum possible score of 129.

- Of the 27 information items included on the disclosure scale:

  - Data on every single item was provided by 4 or more corporations of the 203 studied (not by the same 4, however); and

  - Information on each of 15 items was given by 19% or more of the corporations studied (not by the same corporations in each case, however).

- A Corporation providing these 15 items and no more would have received a "high" score in this assessment. This means that the scoring system is based on the reality of what corporations are already providing to grantseekers and the public.

FINDINGS: **BY SUBJECT AREA**

- More than 60% of the 203 corporations surveyed provided no information on grants made, finances or non-cash (in-kind) contributions, and nearly half (44%) provided no information on governance of their giving programs.

- 16% of the 203 corporations made the maximum score on application and proposal evaluation procedures. But only 1% or less made maximum scores in the other 5 sections: information on kinds of grants possible on grants made, governance, finances and non-cash con butions.

- Over half the corporations scored "high" in providing information on grants possible and application and proposal evaluation procedures. One-quarter scored "high" on grants data. But less than 10% scored "high" on finances and non-cash contributions information.

- Overall the 157 corporations providing any information made some types of data available more readily than others. Below the six subject areas covered in this study are listed in order of corporate preference:

  1. Application and proposal evaluation procedures.
  2. Kinds of grants possible.
  3. Governance of their giving programs.
  4. Information on grants made.
  5. Finances.
  6. Non-cash contributions.

FINDINGS: SIGNIFICANT FACTORS

Corporations with a foundation and a special annual report on their giving program consistently scored highest. This means they provided the most comprehensive information. Of the 47 businesses in this category, none scored zero (i.e. provided no information) and 49% scored "high" (i.e. provided twice as much information as the medium corporation).

- Corporations with no foundation and no annual contributions report generally scored lowest. This means they provided the least amount of information. Of the 93 corporations in this category, 35 (38%) scored zero, and only 1% scored "high".
- Corporations with either a foundation or an annual giving report generally provide more information than corporations with neither and less information than businesses with both.
- But of the two factors, as might be expected, publishing a contributions report is much more likely to lead to a "high" score than simply having a foundation.
- Although having a foundation was much more likely to contribute to a "high" score than not.

SUMMARY/CONCLUSION

The current state of public reporting by corporate philanthropy overall is deplorable. Nearly 1/4 of our largest profit-making corporations refuse to provide any information on their contributions programs when repeatedly requested. And over 30% more score on the low end of an NCRP developed "disclosure scale" which permits assessment of the quality of information provided.

Clearly this scale contains NCRP bias (although much corporate input was sought in devising it). The scale, however, is solidly based in corporate reality. Four or more corporations provided data on every single one of the 27 items used in the scale, and 58 or more businesses (of the 203 studied) made available data on 15 of the items. (The same corporations did not provide information on each and every item, however.) Any corporation providing complete information on these 15 items would have scored "high" on our disclosure scale.

In fact, 27 corporations (13%) did score "high." They show what is possible for all corporations in communicating with grantseekers and the public about their contributions programs.

While the era of openness and disclosure has frequently been declared dead during the Reagan years in the White House, there are important things happening in the nonprofit and public policy world that suggest otherwise. Nevertheless, many corporate philanthropy programs are still in a caveman time warp when it comes to public communication, despite the few who left their caves years ago and are currently light bearers for the rest.

Will traditions of secrecy over R and D efforts, product development and marketing continue to hold corporate philanthropic communications in their bear hug? Or will the models and experience of the 13%, or indeed of the Johnson and Johnson approach to P.R. (ex. Tylenol), or of the continuing thrust of the era of openness and disclosure ultimately succeed in transforming corporate philanthropy into a philanthropy accessible to all, and not just the favored few? I wonder what odds the deposed Jimmy the Greek would offer.

INFORMATION MOST FREQUENTLY PROVIDED

What information was provided by at least 40% of the corporations studied?

(Percentages of the 203 corporations studied which provided this information are listed parenthetically after each item. The weighting of this item for scoring on the "disclosure scale is to the left.)

A. Kinds of Grants Possible

3 1.The purpose of the corporate giving program (56%)

3 2.A detailed statement of program/funding interests/priorities (45%)

6 3.Limitations on funding (58%)

B. Procedures for Application and Evaluation

6 1. Grant application procedures: nature of submission required, person to contact, application deadlines (if any) (62%)

INFORMATION LEAST FREQUENTLY PROVIDED

What information was provided by fewer than 40% of the corporations studied?

(Percentages of the 203 corporations studied which provided this information are listed parenthetically after each item.)

A. Kinds of Grants Possible

3 1.An indication of the amounts available during the current or next year for each program/funding area (4%).

3 2.Policies on length of funding (20%).

B. Procedures for Application and Evaluation

2 1.Proposal evaluation procedures (37%).

1 2.A mention of the length of time for processiong proposals (18%).

C. Information on Grants

4 1.At least a sample list of grants made for one or more recent years (34%).
+4 Fewer corporations provided a grants list for all grants over $5,000 (26%).
+4 And fewer still sent a complete grants list for all grants (16%).

3 2.Names and locations for all grants listed (14%).

3 3.Amounts of all individual grants listed (20%).

3 4.Purposes for all grants listed (8%).

5.Atleast a sample of information on small grants (i.e. names, locations,
4 amounts and/or purposes of grants under $1,000-$5,000)(19%).
Far fewer corporations provided complete information on each small
+2 grant (3%).

3 6.Categorical listing of grants by program area (29%).
Fewer corporations provided also the total grant dollars for each
+3 category (25%).

D. Governance of Corporate Giving Programs

1.List of contribution committee members, foundation directors or
3 other decision-makers (23%).
Far fewer corporations actually identified who these people were
+3 by listing their affiliations or addresses (10%).

6 2.List of staff (14%).

3.Number per year and approximate dates of meetings at which
3 grant decisions are made (14%).

4.Disclosure of where grant decisions are made (i.e. centrally.
6 regionally, or locally in detail sufficient to guide applicant) (38%).

3 5.List of directors and officers of the corporation (14%).

E. Finances

6 1.Total amount granted last year (38%).

2.An indication of whether the total dollars available during the
current year or next year will be the same, more or less, than the
6 past year (4%).

3 3.The total grant amount as a percentage of pretax profits (6%).

3 4.An indication of how the total grant amount was determined (2%).

F. Non-Cash or In-Kind Contributions

1.Brief information on types of non-cash contributions made
3 (merchandise, loaned executives, meeting space, etc.) (26%).
+3 Far fewer corporations provided detailed information of this type (7%).

2.List of non-cash or in-kind contributions for one or more recent
6 years, including names and locations of beneficiaries (4%).
+3 Even fewer corporations identified the type of contribution made (2%)
+3 or the estimated value of the contribution (2%).

6 3.Application procedures (3%).

NOTES

1. AAFRC Trust for Philanthropy, pp. 33 and 49.

2. Ibid.

3. Skrzycki, 1988, citing information provided by Linda Caidillo of the Conference Board in New York City.

4. Olasky, 1987.

5. Ibid.

6. Lydenberg et al, 1986.

7. For more information on this media-philanthropy event, see Stearne, 1987.

8. For more information on this "gran eminences" meeting, see Fox 1987.

9. *Responsive Philanthropy*, Winter 1988.

10. Johnston, 1986.

11. Originally the 200 largest profit-making corporations (from *Forbes* 1985 list) were the objects of study, but one corporation told us it made no contributions from its headquarters, but made them through its four divisions. These four divisions were thus added to the study in place of the headquarters.

12. Bothwell, 1980.

13. The "high" score range was 64 to 98 points out of a maximum 129 on the disclosure scale. Half of the maximum score possible is 64.5 points. Also halfway between the median score (29) and the top actual score (98) is 63.5 points. Thus, 64 was set as the beginning of the "high" score category and 98, the top score achieved by any corporation, is set as its upper limit.

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